United States Court of Appeals

for the Second Circuit

APPENDIX

75-4162

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

B
P/S

No. 75-4162

SEYMOUR SILVERMAN, ET AL.,
Petitioners-Appellants,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee.

APPEAL FROM DECISIONS OF UNITED STATES TAX COURT

APPENDIX

WAGMAN, CANNON & MUSOFF
136 East 57th Street
New York, N. Y. 10022
Attorneys for Petitioners-Appellants

WALLACE MUSOFF
Of Counsel

UNITED STATES COURT OF APPEALS
FILED
OCT 28 1975
A. DANIEL FUSARO, CLERK
SECOND CIRCUIT

PAGINATION AS IN ORIGINAL COPY

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A1

UNITED STATES TAX COURT
GENERAL DOCKET

DOCKET NO. 3707-72

SEYMOUR SILVERMAN

177 Charing Cross

Lynbrook, New York 11563

PETITIONER,

VS.

COMMISSIONER OF INTERNAL REVENUE,

RESPONDENT.

APPEARANCES FOR PETITIONER:

NAME Sidney Gelfand; Stanley P. Wagman; (Gelfand & Radler), 136 East 57th St. New York, New York 10022

ADDRESS Wallace Musoff, 136 East 57th St., New York,N.Y. 10022 E/A 3/27/74)

Date Month Day Year	Filings and Proceedings	Action	Served
May 24, 1972	PETITION FILED: FEE PAID May 24, 1972		May 31,1972
May 24, 1972	REQUEST by petr. for trial at New York, N.Y.	GRANTED May 31,1972	May 31,1972
Jul 21, 1972	ANSWER filed by Resp		Jul 25, 1972
Dec. 20, 1973	Notice of trial on Mar. 18, 1974 at New York, N.Y.		Dec. 20, 1973
Mar.27,& 29, 1974	TRIAL at New York,N.Y. before Judge Quealy.		
	Jt. oral motion for consolidation - (3707-72 thru 3710-72) Granted.		
	Entry of appearance by W. Musoff. filed.		Apr. 19, 1974
	(parties to report on status not later than June 5,1974)		
	STIPULATION OF FACTS and Exh. filed, 1-A thru 10-J. Orally Stipulated, exhibits 11-K thru 14-N.		
	NO BRIEFS DUE		
	SUBMITTED TO JUDGE QUEALY.		
April 16, 1974	TRANSCRIPT of Mar. 27, & 29, 1974 rec'd. (2) vols.		
June 6, 1974	ORDERED, that the parties file simultaneous briefs		JUN 7 1974
	in this case on or before August 5, 1974 and that the		
	parties file reply briefs, If they so wish, on or		
	before September 5, 1974.		
July 31, 1974	MOTION by Resp. to extend time to Aug. 19, 1974 within	GRANTED Aug. 1, 1974	AUG 2 1974
	which to file Brief. (No Obj. Petr.)		

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SEYMOUR SILVERMAN — PETITIONER — PAGE 2

Date	Filings and Proceedings	Action	Served
Aug. 14,1974	BRIEF for Petr. filed.		AUG 20 1974
Aug. 19, 1974	BRIEF for Respondent filed.		AUG 20 1974
Sept. 6, 1974	REPLY BRIEF for petitioner filed.		SEP 20 1974
Sept.19,1974	REPLY BRIEF for Resp. filed.		SEP 20 1974
Nov. 6, 1974	MEMORANDUM FINDINGS OF FACT AND OPINION, Judge Quealy. Decision will be entered under Rule 155.		NOV 6 1974
Nov. 22, 1974	MOTION by Petr. for review by the entire court.	DENIED-See Order 2/5/75	
Nov. 26, 1974	MOTION by Petr. for reconsideration of opinion filed Nov. 6, 1974.	See Order Jan. 29, 1975	
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Dec.11,1974	NOTICE of Objection to Petr.'s Motion for reconsideration of Opinion filed by Resp. to Judge		
Jan. 29,1975	ORDER, that Petr. motion for Reconsideration of Opinion (Opinion filed Nov. 6, 1974; Motion for Reconsideration filed Nov. 26, 1974) is denied.		JAN 30 1975
Feb.5,1975	ORDER, that Petr's motion filed Nov.22,1974 is denied.		FEB 6 1975
May 16, 1975	AGREED COMPUTATION, filed.		
May 20, 1975	DECISION ENTERED, Judge Quealy.		May 20, 1975
	APPELLATE PROCEEDINGS		
July 21, 1975	NOTICE OF APPEAL to U.S.C.A., 2nd Cir., filed by Petrs.		July 22, 1975
July 22, 1975	NOTICE of Filing with copy of notice of appeal sent to Chief Counsel, Mr. Meade Whitaker.		July 22, 1975

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GPO 900.390

UNITED STATES TAX COURT

GENERAL DOCKET

DOCKET NO. 3707-72

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SEYMOUR SILVERMAN — PETITIONER — PAGE 3

Date Month Day Year	Filings and Proceedings	Action	Served
July 22, 1975	NOTICE, to parties, of assembling and date for trans-		
	mission of record.		July 22, 1975

Form No. 34A
March 1957

UNITED STATES TAX COURT
GENERAL DOCKET

DOCKET NO. 3708-72

HELEN SILVERMAN

177 Charing Cross

Lynbrook, New York 11563

PETITIONER,

VS.

COMMISSIONER OF INTERNAL REVENUE,

RESPONDENT.

APPEARANCES FOR PETITIONER:

NAME Sidney Gelfand; Stanley P. Wagman; (Gelfand & Radler) 136 East 57th St., New York, N. Y. 10022

ADDRESS

Date Month Day Year	Filings and Proceedings	Action	Served
May 24, 1972	PETITION FILED: FEE PAID May 24, 1972		May 31,1972
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	thru 3710-72) Granted.		
	Entry of appearance by W.Musoff filed.		Apr. 19.1974
	(parties to report on status not later than		
	June 5,1974)		
	STIPULATION OF FACTS AND Exh. filed, 1-A thru 10-J.		
	Orally Stipulated, exhibits 11-K thru 14-N.		
	NO BRIEFS DUE		
	SUBMITTED TO JUDGE QUEALY		
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HELEN SILVERMAN — PETITIONER — PAGE 2

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UNITED STATES TAX COURT

GENERAL DOCKET

DOCKET NO. 3708-72

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HELEN SILVERMAN — PETITIONER — PAGE 3

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Form No. 34A
March 1957

UNITED STATES TAX COURT
GENERAL DOCKET

DOCKET NO. 3709-72

JACK SILVERMAN
847 Ivy Hill Road
Woodmere, New York 11598
PETITIONER,

VS.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT.

APPEARANCES FOR PETITIONER:
NAME Sidney Gelfand; Stanley P. Wagman; (Gelfand, & Radler), 136 East 57th St., New York, N. Y. 10022
ADDRESS

Date Month Day Year	Filings and Proceedings	Action	Served
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(Continuation)

JACK SILVERMAN — PETITIONER — PAGE 2

Date (Month Day Year)	Filings and Proceedings	Action	Served
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UNITED STATES TAX COURT

GENERAL DOCKET

DOCKET NO. 3709-72

(*Continuation*)

JACK SILVERMAN — PETITIONER — PAGE 3

Date Month Day Year	Filings and Proceedings	Action	Served
July 22, 1975	NOTICE of Filing with copy of notice of appeal sent to		
	Chief Counsel, Mr. Meade Whitaker.		July 22, 1975
July 22, 1975	NOTICE, to parties, of assembling and date for trans-		
	mission of record.		July 22, 1975

GPO : 1973—O-496-979

UNITED STATES TAX COURT
GENERAL DOCKET

DOCKET NO. 3710-72

FRANCES SILVERMAN
847 Ivy Hill Road
Woodmere, New York 11598
PETITIONER,

VS.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT.

APPEARANCES FOR PETITIONER:
NAME Sidney Gelfand; Stanley P. Wagman; (Gelfand & Radler), 136 East 57th St., New York N. Y. 10022
ADDRESS

Date Month Day Year	Filings and Proceedings	Action	Served
May 24, 1972	PETITION FILED: FEE PAID May 24, 1972		May 31,1972
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	Jt. oral motion for consolidation (3707-72		
	thru 3710-72) Granted.		
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	Orally Stipulated, exhibits 11-K thru 14-N.		
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June 6,1974	ORDERED, that the parties file simultaneous briefs		JUN 7 1974
	in this case on or before August 5, 1974 and that the		
	parties file reply briefs, if they so wish, on or		
	before September 5, 1974.		
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DOCKET NO. 3710-72 A11

(Continuation)

FRANCES SILVERMAN — PETITIONER — PAGE 2

Date (Month Day Year)	Filings and Proceedings	Action	Served
July 31, 1974	MOTION by Resp. to extend time to Aug. 19, 1974 within which to file Brief. (No Obj. Petr.)	GRANTED Aug. 1, 1974	AUG 2 1974
Aug.14,1974	BRIEF for Petr. filed.		AUG 20 1974
Aug. 19, 1974	BRIEF for Respondent, filed.		AUG 20 1974
Sept. 6, 1974	REPLY BRIEF for petitioner filed.		SEP 20 1974
Sept.19,1974	REPLY BRIEF for Resp. filed.		SEP 20 1974
Nov. 6, 1974	MEMORANDUM FINDINGS OF FACT AND OPINION, Judge Quealy. Decision will be entered under Rule 155.		NOV 6 1974
Nov. 22, 1974	MOTION by Petr. for Review by the Entire Court.	DENIED-See Order 2/5/75	
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Nov. 26, 1974	MOTION by Petr. for additional findings of fact.	DENIED Nov. 26, 1974	NOV 27 1974
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Dec.11,1974	NOTICE of Objection to Petr.'s Motion for reconsideration of Opinion filed by Resp.	To Judge	
Jan. 29, 1975	ORDER, that Petr. motion for Reconsideration of Opinion (Opinion filed Nov. 6, 1974; Motion for Reconsideration filed Nov. 26, 1974) is denied.		JAN 30 1975
Feb.5,1975	ORDER, that Petr's motion filed Nov.22,1974 is denied.		FEB 6 1975
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May 20, 1975	DECISION ENTERED, Judge Quealy.		May 20, 1975
	APPELLATE PROCEEDINGS		
July 21, 1975	NOTICE OF APPEAL to U.S.C.A., 2nd Cir., filed by Petrs.		July 22, 1975

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UNITED STATES TAX COURT

GENERAL DOCKET

DOCKET NO. 3709-72

(*Continuation*)

FRANCES SILVERMAN — PETITIONER — PAGE 3

Date Month Day Year	Filings and Proceedings	Action	Served
July 22, 1975	NOTICE of Filing with copy of notice of appeal sent to Chief Counsel, Mr. Meade Whitaker.		July 22, 1975
July 22, 1975	NOTICE, to parties, of assembling and date for transmission of record.		July 22, 1975

GPO : 1973—O-496-979

UNITED STATES TAX COURT

SEYMOUR SILVERMAN, Petitioner, v. COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	Docket No. 3707-72
HELEN SILVERMAN, Petitioner, v. COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	Docket No. 3708-72
JACK SILVERMAN, Petitioner, v. COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	Docket No. 3709-72
FRANCES SILVERMAN, Petitioner, v. COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	Docket No. 3710-72

STIPULATION OF FACTS

The parties hereby stipulate and agree that for the purpose of these cases the following facts and exhibits attached hereto

and made a part hereof may be taken as true, subject to the rights of the parties to introduce other and further evidence not inconsistent with this stipulation and preserving the parties' rights to object, at the time of trial, to any and all portions of said stipulation and attached exhibits as they may deem to be irrelevant or immaterial.

1. Petitioners, Seymour Silverman and Helen Silverman, are husband and wife and at the time of the filing of their petitions herein, they legally resided at 177 Charing Cross, Lynbrook, New York. Seymour Silverman filed a U.S. Gift Tax return for the calendar year 1968 with the District Director of Internal Revenue, Brooklyn, New York. Helen Silverman consented to have the gifts made during the calendar year 1968 considered as having been made one-half by her and the other half by her spouse, Seymour Silverman. Attached hereto and marked Exhibit 1-A is a copy of the Gift Tax return filed by Seymour and Exhibit 2-B is a copy of the Gift Tax return filed by Helen.

2. Petitioners, Jack Silverman and Frances Silverman, are husband and wife and at the time of the filing of their petitions herein, they legally resided at 847 Ivy Hill Road, Woodmere, New York. Jack Silverman filed a U.S. Gift Tax return for the calendar year 1968 with the District Director of Internal Revenue, Brooklyn, New York. Frances Silverman consented to have the gifts made during the calendar year 1968 considered as having been

made one-half by her and the other half by her spouse, Jack Silverman. Attached hereto and marked Exhibit 3-C is a copy of the Gift Tax return filed by Jack and Exhibit 4-D is a copy of the Gift Tax return filed by Frances.

3. Modern Maid Food Products, Inc. was organized on January 7, 1952 under the laws of the State of New York and has engaged in the business of manufacturing and selling breadings and batter mixes for use by processors of shrimp, fish and poultry, and the manufacturing and selling prepared flour mixes for mass feeding outlets such as hospitals, restaurants and hotels. The flour mixes are sold through wholesale grocers. Modern Maid Food Products, Inc. is a successor to a partnership formed in 1933.

4. On April 22, 1968 Modern Maid Food Products, Inc. requested a ruling from the Commissioner of Internal Revenue with respect to a proposed reorganization. Said request for ruling is attached as Exhibit 5-E.

5. On June 28, 1968 the Commissioner of Internal Revenue issued his ruling with respect to the request made on April 22, 1968. Said ruling is attached as Exhibit 6-F.

6. On August 11, 1968 the outstanding capital stock of Modern Maid Food Products, Inc. was held as follows:

	Common Stock $100 Par Value	Preferred Stock $100 Par Value
Jack Silverman	1,284	265
Seymour Silverman	645	430
Harold Oppenheim	225	150
Stanley Silverman	3	10
Jack Silverman	3	10
Jack Silverman Foundation		575
	2,160	1,440

7. Modern Maid Food Products, Inc. voted to adopt the proposed plan of reorganization on July 13, 1968 which became effective on August 12, 1968. On the latter date the outstanding capital stock of Modern Maid Food Products, Inc. was held as follows:

	Class A Common $10 Par Value	Class B Common $10 Par Value	5% Common Preferred Stock $100 Par Value
Jack Silverman	12,840	51,360	14,389
Seymour Silverman	6,450	25,800	7,525
Harold Oppenheim	2,250	9,000	2,625
Stanley Silverman	30	120	43
Joel Silverman	30	120	43
Jack Silverman Foundation			575
	21,600	86,400	25,200

8. Balance Sheet of Modern Maid Food Products, Inc. at December 31, 1967 attached as Exhibit 7-G..

9. Consolidated Balance Sheet of Modern Maid Food Products, Inc. at December 31, 1967 attached as Exhibit 8-H.

10. Consolidated Statement of Operations of Modern Maid Food Products, Inc. for calendar years 1964 through 1967 attached as Exhibit 9-I.

11. The following gifts of Class B common stock were made:

Date	Donor	Donee	No. of Shares
8/21/68	Jack Silverman	Trust for Benefit of Joel Silverman	25,680
		Trust for Benefit of Stanley Silverman	25,680
9/24/68	Seymour Silverman	Trust for Benefit of Susan Silverman	8,600
		Trust for Benefit of Anne Silverman	8,600
		Trust for Benefit of Beth Silverman	8,600
12/8/68	Harold Oppenheim	Martin Oppenheim	2,000
		Sandra Oppenheim	2,000
		Trust for Benefit of Elysia Beth Oppenheim	2,000
		Trust for Benefit of Robert Alan Oppenheim	2,000

12. Modern Maid Food Products, Inc. made the following sales of original issue Class B common stock in September, 1968 at $10 per share, pursuant to an agreement in August, 1968:

Name	No. of Shares	Position	Approximate 1968 Remuneration
Hercules Adams	200	Salesman	$28,000
Ron Bronsweig	200	Plant Manager	17,000
Tony Cimorelli	200	Asst. Maintenance Manager	11,500
Latif Elias	100	Salesman	33,000
Robert Fussell	100	Salesman	31,000
Joshua Hoffman	200	Outside Management Consultant	
Arthur Jaspan	90	Member of Law Firm	
Joseph Jaspan	400	Member of Law Firm	
William Lipton	200	Salesman	50,000
Martin Luck	400	Salesman	28,000
Minnie Miller	300	Bookkeeper	9,500
Michael Piccirillo	400	Foreman - Maintenance	19,000
Eddie Soregaroli	400	Production Foreman	12,000
Joe Silverman	800	Traffic Manager	12,000
Neil Trager	200	Head of Research Lab.	12,000
Arthur Ulman	200	Salesman	20,000
John Urban	400	Vice President - Processing Div.	26,000

13. A schedule of dividends paid by Modern Maid Food Products, Inc. in 1964 through 1968 is attached as Exhibit 10-J.

14. If the parties' expert appraisal witnesses were questioned as to their experience, their testimony would be as set forth in their respective appraisal reports.

Counsel for Petitioners.

MEADE WHITAKER
Chief Counsel
Internal Revenue Service.

MAR 2 7 1974

By: (sgd) THEODORE E. DAVIS - EHH
THEODORE E. DAVIS
Assistant Regional Counsel

OF COUNSEL:
MARVIN E. HAGEN
Regional Counsel
STANLEY J. GOLDBERG
Attorney
Internal Revenue Service
26 Federal Plaza (12th Floor)
New York, New York 10007.
Tel. No. 212-264-0270

April 22, 1968.

Commissioner of Internal Revenue
Washington, D.C. 20025.

ATT: Taxpayers Ruling Section
Reorganization Branch.

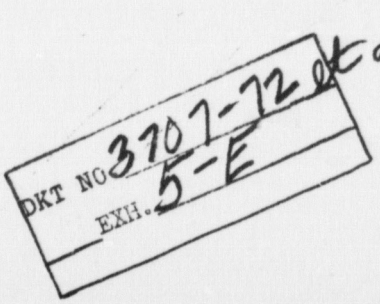
Dear Sir:

A ruling is requested that the following proposed plan of recapitalization of Modern Maid Food Products, Inc. of 110-60 Dunkirk Street, Jamaica, New York, 11412, qualifies as a reorganization under Section 368(a)(1)(E) and that no gain or loss is recognized to the Corporation or its shareholders pursuant to Section 354 of the Internal Revenue Code of 1954.

The present capitalization of Modern Maid Products, Inc. and the shares held by respective shareholders are as follows:

	Common Stock Par Value $100	Preferred Stock Par Value $100
Jack Silverman	1284	265
Seym our Silverman	645	430
Harold Oppenheim	225	150
Stanley Silverman	3	10
Joel Silverman	3	10
Jack Silverman Foundation, Inc.		575
	2160	1440
Authorized	5000	1500

The Corporation has from time to time considered the advisability of selling stock to various employees and business related individuals, which management believes would greatly benefit the Corporation and assure its continued growth and success. Such plans have been deferred due to large equity interest in the common stock and the relative small percentage of interest that would flow to the employees. Such condition has not permitted an offer of stock to be sufficiently attractive to serve as an incentive to contemplated purchasers.



Commissioner of Internal Revenue

ATT: Taxpayers Ruling Section
Reorganization Branch

Messrs Jack & Seymour Silverman and Harold Oppenheim, on the other hand, have been receiving only a nominal return on their investment due to financial demands of an expanding corporate business, and are anxious to obtain a fixed return on their investment.

It is intended to recapitalize Modern Maid Food Products, Inc. by increasing authorized preferred stock $100 par value from 1500 shares to 30,000 shares and create two new classes of stock:

a) 24,000 shares voting Class A common stock - Par Value $10 a share.

b) 96,000 shares non-voting Class B common stock - Par Value $10 a share.

An exchange of stock would then be made as follows:

1. Each share of presently owned common stock, par value $100 per share, would be exchanged for

a. 10 shares Class A common- New
b. 40 shares Class B " "
c. 11 shares Preferred

At December 31, 1967 the Consolidated Net Worth of Modern Maid Food Products, Inc. and Subsidiary Corporations was:

Common stock	216,000
Preferred stock	144,000
Surplus	3,491,000
	3,851,000

April 22, 1966

Commissioner of Internal Revenue

ATTN: Taxpayers Ruling Section
Reorganization Branch

After the proposed recapitalization the capitalization and shareholder holdings would be

	Class A Common $10 Par Value	Class B Common $10 Par Value	Preferred Stock $100 Par Value
Jack Silverman	12,800	51,300	14,389
Seymour Silverman	6,450	25,800	7,525
Harold Oppenheim	2,250	9,000	2,625
Stanley Silverman	30	120	43
Joel Silverman	30	120	43
Jack Silverman Foundation, Inc.			375
	21,600	86,400	25,200

The Net Worth would be represented by the following:

Class A Common Stock	$ 216,000
Class B " "	864,000
Preferred Stock	2,520,000
Surplus	231,000
	$3,831,000

Each 100 shares of Class B stock to be sold for $1000 would have approximately the same book value and would represent a .0026% in the common equity and growth of the company. This should present an investment opportunity sufficiently attractive to approximately 30 employees and business related individuals to provide an incentive and at a price low enough to enable them to participate in corporate growth. Under present capitalization $1000 would represent only a .027% in common equity.

The taxpayer identification numbers of interested parties are:

Modern Maid Food Products, Inc.	No.	11-1000003
Jack Silverman	"	073-01-0529
Seymour Silverman	"	033-18-0178
Harold Oppenheim	"	140-07-7339
Stanley Silverman	"	030-36-1507
Joel Silverman	"	070-02-2301
Jack Silverman Foundation, Inc.	"	11-1007033

-2-

April 21, 1961

Commissioner of Internal Revenue

ATTN: Taxpayers Ruling Section
Reorganization Branch

There are enclosed herewith balance sheets of Modern Maid Food Products, Inc., and a consolidated balance sheet of Modern Maid Food Products, Inc. and subsidiaries, both as of December 31, 1960.

Also enclosed is a memorandum of law setting forth taxpayer's position with respect to applicable law.

We would appreciate your expeditious action on this requested ruling and would and welcome your calling collect for any information desired. We are also prepared to discuss any phase of the issue at your convenience in Washington, D.C.

Powers of Attorney and copies of presently executed stock certificates are enclosed.

Respectfully yours,

[redacted]

_____
Stanley Goldstein

Encs
cc:

MODERN MAID FOOD PRODUCTS, INC.
Balance Sheet
December 31, 1967.

A S S E T S

CURRENT ASSETS		
Cash	472,524	
Accounts & Notes Receivable	2,656,444	
Inventories	415,458	
Certificate of Deposit	150,000	
Interest Receivable	4,029	
		3,698,455
FIXED ASSETS		
Machinery & Equipment	808,980	
Furniture & Fixtures	86,726	
Leasehold Improvements	208,059	
	1,103,765	
Less: Reserve for Depreciation	576,880	
		526,885
OTHER ASSETS		
Due from Subsidiary Corp.	411,605	
Investment in Subsidiary	70,000	
Deposits & Advances	49,383	
Investments	26,000	
Life Insurance- Cash Surrender Value	32,703	
Deferred Charges	4,221	
Net Leasehold	3,950	
		597,862
		$ 4,823,202

LIABILITIES & CAPITAL

CURRENT		
Accounts Payable	744,138	
Taxes Withheld	23,570	
Accrued Expenses	212,249	
Federal Income Taxes	205,838	
Due Officers	21,901	
Notes Payable	36,455	
		1,244,151
NET WORTH		
Common Stock	216,000	
Preferred Stock	144,000	
Surplus	3,219,051	
		3,579,051
		$ 4,823,202

MODERN MAID FOOD PRODUCTS, INC.
and Subsidiary Corporations
Consolidated Balance Sheet
December 31, 1967.

ASSETS		
CURRENT		
Cash	$ 497,715	
Accounts & Notes Receivable	2,656,444	
Inventories	415,458	
Certificate of Deposit	150,000	
Interest Receivable	4,029	$3,723,646
FIXED ASSETS		
Machinery & Equipment	1,636,987	
Furniture & Fixtures	87,927	
Leasehold Improvements	220,959	
Land & Building	343,358	
Truck Trailer	24,842	
	2,314,074	
Less: Reserve for Depreciation	1,039,470	1,274,604
OTHER ASSETS		
Deposits & Advances	54,027	
Investments	26,000	
Life Insurance - Cash Surrender Value	32,703	
Deferred Charges	13,415	
Net Leasehold	3,950	130,095
		$5,128,345
LIABILITIES & CAPITAL		
CURRENT		
Accounts Payable	744,138	
Taxes Withheld	25,036	
Accrued Expenses	237,496	
Federal Income Taxes	211,999	
Due to Officers	21,901	
Notes Payable	36,455	$1,277,025
NET WORTH		
Common Stock	216,000	
Preferred Stock	144,000	
Surplus	3,491,320	3,851,320
		$5,128,345

Internal Revenue Service

Date: JUN 27 1968 | In reply refer to: T:I:R:2

Modern Maid Food Products, Inc.
110-60 Dunkirk Street
Jamaica, New York 11412

Gentlemen:

This is in reply to a letter dated April 22, 1968, in which a ruling is requested as to the Federal income tax consequences of a proposed transaction. Additional information was submitted in a letter dated June 18, 1968. The relevant facts submitted for consideration are substantially as set forth below.

Modern Maid Food Products, Inc. ("Company"), employer identification number 11-1690883, is a New York corporation engaged in the food business. As of April 22, 1968, it had outstanding 2160 shares of voting common stock ("Old Common Stock"), and 1440 shares of five percent cumulative nonvoting preferred stock ("Preferred Stock") par value $100. The two classes of stock were held as follows:

Name and Taxpayer Account Number	Old Common Stock	Preferred Stock
Jack Silverman 073-28-6529	1284	265
Seymour Silverman 062-16-0978	645	430
Harold Oppenheim 140-07-7659	225	150
Stanley Silverman 084-34-1567	3	10
Joel Silverman 076-32-2391	3	10
Jack Silverman Foundation, Inc. 11-6037023		575
	2160	1440

It is desired to give the three major holders of Old Common Stock greater opportunity to obtain a fixed return on their investment, and also it is desired to increase the attractiveness of Company's common

3707-72 et al
6-F

stock as a growth investment. Accordingly, pursuant to a plan, it is proposed that the following steps be taken. The authorized number of shares of Preferred Stock will be increased. Two new classes of stock will be created: voting Class A common stock ("Class A Stock"); and nonvoting Class B common stock ("Class B Stock"). These two new classes of common stock will not be redeemable, and will be identical in all respects except that the Class B Stock will be nonvoting. Thereafter, each share of the presently outstanding Old Common Stock will be exchanged for a total of 10 shares of Class A Stock, 40 shares of Class B Stock, and 11 shares of Preferred Stock. Following this exchange the outstanding stock of Company will be held as follows:

	Class A Stock	Class B Stock	Preferred Stock
Jack Silverman	12,840	51,360	14,389
Seymour Silverman	6,450	25,800	7,525
Harold Oppenheim	2,250	9,000	2,625
Stanley Silverman	30	120	43
Joel Silverman	30	120	43
Jack Silverman Foundation, Inc.			575
	21,600	86,400	25,200

There are no plans for the sale or other disposition of the stock to be received in the proposed transaction, except that it is possible that there may be some gifts of Class B Stock. It is represented that no more than 50 percent of the total equity interest to be received in the transaction will be the subject of any such gifts.

Company and its shareholders will each pay their own expenses arising out of the proposed transaction.

Based solely on the information submitted, it is held as follows:

(1) The proposed exchange by shareholders of Company of all of their Old Common Stock for Class A Stock, Class B Stock, and Preferred Stock, as described above, will constitute a recapitalization and therefore a reorganization within the meaning of section 368(a)(1)(E) of the Internal Revenue Code of 1954.

(2) No gain or loss will be recognized to Company on the receipt of its Old Common Stock in exchange for its Class A Stock, Class B Stock, and Preferred Stock.

(3) No gain or loss will be recognized to the shareholders of Company upon the exchange of their Old Common Stock for Class A Stock, Class B Stock, and Preferred Stock (section 354(a)(1)).

(4) The basis of the Class A Stock, Class B Stock, and Preferred Stock received by the Company shareholders in exchange for their Old Common Stock is for each shareholder the same as the basis of the Old Common Stock surrendered by such shareholder in exchange therefor (section 358(a)(1)). Such basis should be allocated among the shares of Class A Stock, Class B Stock, and Preferred Stock in proportion to their respective fair market values on the date of the exchange (section 358(b) of the Code and section 1.358-2(a)(2) of the Regulations).

(5) The Preferred Stock received in the exchange will constitute "section 306 stock" within the meaning of section 306(c).

(6) Regardless of any book entries made, the consummation of the proposed transaction will not diminish the earnings and profits of Company available for distribution of dividends within the meaning of section 316 of the Code (section 312(d)).

No opinion is expressed as to the tax treatment of the transaction under the provisions of any of the other sections of the Code and Regulations which may also be applicable thereto, or to the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction which are not specifically covered by the above rulings.

A copy of this letter should be attached to the Federal income tax returns of the parties involved for the taxable year in which the transaction covered by this ruling is consummated.

Pursuant to a power of attorney on file in this office, a copy of this ruling is being sent to Mr. Sidney Golfand.

Very truly yours,

John F. Bogaard

Chief, Reorganization Branch

MODERN MAID FOOD PRODUCTS INC.
Balance Sheet
December 31, 1967

ASSETS

Current Assets		
Cash	472,524	
Accounts & Notes Receivable	2,656,444	
Inventories	415,458	
Certificate of Deposit	150,000	
Interest Receivable	4,029	
		3,698,455
Fixed Assets		
Machinery & Equipment	808,980	
Furniture & Fixtures	86,726	
Leasehold Improvements	208,059	
	1,103,765	
Less Reserve for Depreciation	576,880	
		526,885
Other Assets		
Due from Subsidiary Corp.	411,605	
Investment in Subsidiary	70,000	
Deposits & Advances	49,383	
Investments	26,000	
Life Insurance - Cash Surrender Value	32,703	
Deferred Charges	4,221	
Net Leasehold	3,950	
		597,862
		4,823,202

LIABILITIES & CAPITAL

Current		
Accounts Payable	744,138	
Taxes Withheld	23,570	
Accrued Expenses	212,249	
Federal Income Taxes	205,838	
Due Officers	21,901	
Notes Payable	36,455	
		1,244,151
Net Worth		
Common Stock	216,000	
Preferred Stock	144,000	
Surplus	3,219,051	
		3,579,051
		4,823,202

Docket No. 3707-72, et al.
Exh. 7-G

MODERN MAID FOOD PRODUCTS INC.
Schedule of Dividends Paid

Date	Preferred	Common
1964		
April	900	--
June	900	--
Sept.	900	18,000
Dec.	900	
	3,600	18,000
1965		
March	1,800	--
June	1,800	
Sept.	1,800	28,800
Dec.	1,800	
	7,200	28,800
1966		
April	1,800	--
July	1,800	--
Oct.	1,800	36,000
Dec.	1,800	
	7,200	36,000
1967		
April	1,800	--
June	1,800	--
Sept.	1,800	--
Nov.		37,800
	5,400	37,800
1968		
Feb.	1,800	--
April	1,800	--
June	1,800	--
Sept.	12,492	--
Dec.	31,500	--
	49,392	-0-

Docket No. 3707-72, et al.
Exh. 10-J

CERTIFICATE OF AMENDMENT
OF
CERTIFICATE OF INCORPORATION
OF
MODERN MAID FOOD PRODUCTS, INC.

Pursuant to Section 805 of the Business Corporation Law.

We, the undersigned, the holders of all of the outstanding shares of stock of MODERN MAID FOOD PRODUCTS, INC., entitled to vote thereon, hereby certify

1. The name of the corporation is MODERN MAID FOOD PRODUCTS, INC.

2. The Certificate of Incorporation was filed in the office of the Secretary of State on January 7, 1952.

3. The Certificate of Incorporation was amended on November 21, 1962 to increase the stated amount of capital stock of the corporation to $650,000.00 and to increase the number of authorized shares by authorizing 1500 shares of preferred stock with a par value of $100.00 each, in addition to the previously issued stock of 5000 shares of common stock with a par value of $100.00 each.

4. The Certificate of Incorporation is further amended as authorized by Section 801 of the Business Corporation Act to effect the following amendments:

(a) To increase the total number of shares which the corporation is to be authorized to issue.

(b) To remove from the authorized shares the present shares of common stock $100.00 par value, whether issued or unissued.

(c) To create a new issue of Common Stock Class A of $10.00 par value.

DKT NO. 3762-12
EXH. 13-M

(d) To create a new issue of non-voting Common Stock Class B. $10.00 par value.

(e) To increase the number of shares of the currently authorized Preferred Stock $100.00 par value.

(f) To increase the stated capital of the corporation from $650,000.00 to $4,200,000.00.

5. To accomplish such amendments the Certificate of Incorporation, as amended, shall contain statements with respect to the authorized shares, as hereby amended to read as follows:

(a) The amount of capital stock which the corporation is hereafter to have is $4,200,000.00.

(b) The total number of shares, including those shares of preferred stock previously authorized, which the corporation might hereafter have is 150,000 shares of stock consisting of 24,000 shares of Class A Common Stock at a par value of $10.00 each. 96,000 shares of Class B Common Stock at a par value of $10.00 each, and 30,000 shares of preferred stock at a par value of $100.00 each.

(c) Except as otherwise provided by law or this Certificate of Incorporation, the holders of shares of Class A Common Stock shall have and possess the exclusive right to notice of stockholders meetings, and the exclusive voting rights and powers, and the holders of Class B Common Stock shall not be entitled to notice of stockholders meetings or to vote upon the election of directors or upon any questions affecting the management or affairs of the corporation, except where such notice or vote is required by law or by this Certificate of Incorporation.

(d) The provision of this Certificate of Incorporation which authorizes the issuance of 5000 shares of common stock at a par value of

$100.00 each, all of one class, is eliminated.

(c) The provision in this Certificate of Incorporation which authorizes the issuance of 1500 shares of the Preferred Stock and designates preferences, privileges, voting powers and restrictions thereof, is amended only to the extent that the number of preferred shares of stock which the corporation is authorized to issue is increased from 1500 shares of Preferred Stock at a par value of $100.00 each to 30,000 shares of Preferred Stock at a par value of $100.00 each.

6. The amendment of the Certificate of Incorporation is authorized by the unanimous written consent, setting forth the action taken, signed by the holders of all outstanding shares entitled to vote thereon.

IN WITNESS WHEREOF, we have executed this Certificate and affirmed the truth of the statements herein set forth under penalty of perjury this 13 day of July, 1968.

Jack Silverman

Seymour Silverman

Harold Oppenheim

Joel Silverman

Stanely Silverman

AGREEMENT RESTRICTING SALE OF CERTAIN SHARES OF CLASS B NON-VOTING STOCK OF MODERN MAID FOOD PRODUCTS, INC.

WHEREAS, the undersigned persons are associated with and/or employed by MODERN MAID FOOD PRODUCTS, INC., (hereinafter called the "Corporation"), and have agreed upon the execution of a subscription for or upon the purchase of Class B non-voting common shares of the Corporation, to certain restrictions and obligations on themselves, the Corporation and the shares of stock of the Corporation,

IT IS, THEREFORE, AGREED:

1. Purchase for Investment Purposes Only: The undersigned individuals, each of whom has subscribed for or purchased Class B non-voting shares of common stock of the Corporation, do hereby acknowledge that all of the shares acquired or being acquired by them will be beneficially owned and acquired by them for investment only, with no present intention of public distribution.

2. Restriction on Stock: No stockholder who shall subscribe to this agreement shall dispose of or encumber any part of his Class B non-voting common stock, except under the following conditions:

(a) The party desiring to dispose of or encumber his stock must first obtain the written consent of the Board of Directors of the Corporation.

(b) In the absence of such written consent, the party desiring to dispose of or encumber his stock shall give to the Corporation written notice by certified mail of his intention, and such notice shall contain an offer to sell all his stock in accordance with the terms of this agreement. Within thirty (30) days after the date of such notice, the stockholder giving such notice shall sell and the Corporation shall purchase all of such stockholder's stock.

DKT NO. 3707-72 et al
EXH. 14-N

The purchase price of each share of stock shall be based upon the value shown on the last Federal Income Tax Return (or if such information is not available in said return, the annual financial statement) or any other value as set by agreement between the parties. The purchase price shall be paid in cash. If, at the time the corporation is required to make payment of the purchase price, its surplus is insufficient for such purpose, then the entire available surplus shall be used to purchase part of such stock and the holders of Class A common stock of the Corporation, in proportion to their holdings of such stock,shall within sixty (60) days after the date of the original notice purchase and such stockholders shall sell the unpurchased stock. Payments for the stock so purchased shall be made in cash at the value set forth above.

3. Purchase of Stock on Death: Upon the death of any holder of Class B non-voting common stock of the Corporation, all of his said stock shall be purchased in the manner set forth in paragraph 2(b) of this agreement. The estate shall be obligated to offer such stock for sale as herein provided and such offer shall be made or deemed to be made within thirty (30) after the qualification of a legal representative of such estate. The time within which the Corporation, and if necessary, the Class A stockholders of the Corporation shall purchase and pay for the stock shall not commence to run until the Corporation shall have received written notice by certified mail of the appointment of the legal representative, but nothing shall prevent the consummation of the sale and purchase of said stock at the option of the Corporation or the Class A stockholders, as the case may be, in advance of or in the absence of such written notice.

4. Retirement or Termination of Employment of Stockholder: Upon the retirement of any employee of the corporation subscribed hereto, or upon the termination of his employment, he shall be deemed to have

offered all of his stock, for sale upon the terms and conditions and in the manner set forth in paragraph 2(b) of this agreement.

5. Endorsement on Stock Certificates: All certificates of Class B common stock of the Corporation affected by this agreement shall be endorsed:

> This certificate is transferable only upon compliance with the provisions of an agreement dated August 12, 1968, a copy of which is on file in the Office of the Secretary of the Corporation.

6. Limited Application of this Agreement: This agreement is intended to apply only to the Class B common stock of the Corporation sold by the Corporation to the undersigned parties and does not limit the alienability of nor affect such Class B stock as may have been received by holders of common stock pursuant to a recent plan of recapitalization on file with the secretary of the Corporation, except as such alienability may be limited by other agreements then in existence.

7. Documentary Stamps: Whenever any stock is sold pursuant to this agreement, the seller shall affix to the certificate of stock the necessary documentary stamps.

8. Notice: All notices to the Corporation shall be sent to 110-60 Dunkirk Street, Jamaica, New York. Notice to other parties to this agreement shall be sent to the last known addresses as they appear on the records of the Corporation.

9. Benefit: This agreement shall be binding upon the parties, their heirs, legal representatives, successors and assigns.

10. Counterparts: This agreement may be executed at the end of the original hereof or any copy thereof and shall be effective as of the date of execution thereof.

IN WITNESS WHEREOF, the parties hereto have executed this agreement.

Dated: August [illegible], 1968.

MODERN MAID FOOD PRODUCTS, INC.

By _____

CLASS B STOCKHOLDERS	Number of Shares	Date
[illegible]	[illegible]	[illegible]
[illegible]		
Harold W. Brosmith	[illegible]	[illegible]

The undersigned, holders of Class A Common Stock of MODERN MAID FOOD PRODUCTS, INC., do hereby execute this agreement for the sole purpose of binding themselves to the obligation to purchase the shares of Class B Common Stock which the Corporation in the absence of an adequate surplus may not purchase.

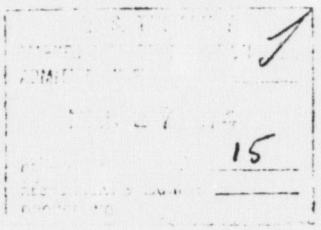
Jack Silverman

Seymour Silverman

Harold Oppenheim

Joel Silverman

Stanley Silverman



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MINUTES OF MEETING OF THE BOARD OF DIRECTORS

-of-

MODERN MAID FOOD PRODUCTS, INC., HELD AT THE OFFICE OF THE CORPORATION, 110-60 DUNKIRK STREET, JAMAICA, NEW YORK, on the 6th day of DECEMBER, 1968 at 10:00 A. M.

PRESENT: FRANCES SILVERMAN
JACK SILVERMAN
SEYMOUR SILVERMAN

Jack Silverman acted as Chairman and Seymour Silverman acted as Secretary.

By motion duly made and unanimously adopted, the following persons were elected as officers of the Corporation:

Jack Silverman - President
Harold Oppenheim - Vice-President
John Urban - Vice-President
Seymour Silverman - Secretary-Treasurer

By motion duly made and carried, the officers were authorized to file resolutions with the respective banks providing for withdrawals upon the sole signature of any one of the following: President, Secretary or Stanley Silverman as authorized signatory.

By motion duly made and carried, it was unanimously voted that the corporation should contribute the sum of $150,000.00 to the Profit Sharing Plan maintained for the benefit of the employees of the corporation.

A discussion followed as to the plans for expansion into the Canadian area, and particularly with respect to serious talks under way with Reid Milling Limited. It was pointed out that the corporation may be required to make a substantial investment since the operation in Streetsville, Ontario Province, Canada, will involve the construction of a building and the necessary equipment for a breading operation. In view of the heavy expenditures involved in the modernization of the existing plant, it may become necessary to arrange some financing before proceeding with the Canadian proposal. In any event, all problems associated with it are being checked out and there will shortly be a conference in New York with the

representatives of Reid Milling Limited to move this matter. The directors authorized Jack Silverman, as president, to enter into such preliminary agreements as he may deem necessary for the purpose of concluding this project.

There being no further business the meeting was adjourned.

Dated: December 6, 1968.

Secretary

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STREETSVILLE • ONTARIO • TELEPHONE 2784101 OR 678-6101

October 26, 1968

Mr. Jack Silverman, President,
Modern Maid Food Products Inc.,
110 - 60 Dunkirk Street,
Jamaica, N.Y. 11412

Dear Mr. Silverman:

I was so pleased to have you, Mr. Urban and Mr. Jaspan with me last Wednesday. I felt that our discussions were frank and meaningful and that a great deal of ground was covered in our one day together. Certainly it would seem that we have the 'makings' of a good deal.

The first part of next week I will be in Montreal but immediately upon my return I will pull together the information requested during our discussions and send it along. Sorry for the delay but sales matters must come first. In the meantime I trust that you and Mr. Urban are following up with market surveys of the US, estimated costs of equipment, building layout, etc.

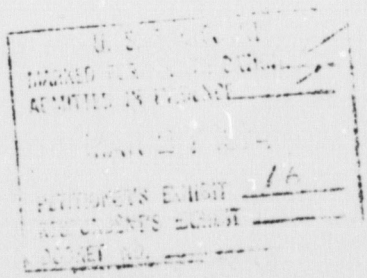
I will be writing again shortly.

Best regards.

Sincerely,

PBH/sc

P.B. Helliwell



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Ex. 17

Appraisal
Modern Maid Food Products, Inc.
Class "B" Common Stock
1968

HAROLD M. WIT
30 BROAD STREET
NEW YORK, N.Y. 10004

March 25, 1974

Mr. Sidney Gelfand
Gelfand & Radler
136 East 57th Street
New York, New York

Dear Mr. Gelfand:

In accordance with your request, I have determined that a willing and knowledgeable purchaser would have paid no more than $5 to $6 per share for Class "B" Common Stock of Modern Maid Food Products Inc. in August and September 1968.

I am attaching to this letter a report, which includes the following headings:

1. Qualifications
2. Basis of Appraisal
3. Valuation Opinion

Very truly yours,

Harold M. Wit

HMW:ri

Enclosure

QUALIFICATIONS - HAROLD WIT

Education:

1949	Harvard College	A.B.
1954	Yale University Law School	J.D.

Business History:

1954	Admitted to New York Bar
1954-1958	Lawyer with Cravath, Swaine & Moore, N.Y.City
1958-1960	One William Street Fund
1960-1974	Allen & Co & Allen & Co., Inc.-Investment Bankers

Directorships, etc.

Grey Advertising Co.	Listed over-the-counter
DPF, Inc.	" N.Y. Stock Exchange
Raymond Control Systems	
I. Wit Realty Corp.(President)	Private real estate and securities investing company

Trustee of several family trusts which own and invest in publicly held securities.

Business Experience:

With Cravath, Swaine & Moore worked on commercial non-litigation matters, particularly those relating to registration and sale of securities to the public

With One William Street Fund, a diversified open end mutual fund managed by Lehman Brothers, I was concerned almost exclusively with administrative and legal matters relating to the operation of the Fund. I was present at Booard and Executive Committee meetings at which investment strategy and decisions were discussed and passed on. When I left the One William Street Fund in 1960, I was vice-president and secretary of the Fund.

With Allen & Co , I am engaged in investigating

investment opportunities for the firm for investing its own funds in private and public situations. I am primarily a "new business" man in a "merchant banking" firm. I am responsible for watching situations in which investments were made upon my recommendations.

As Executive Vice-President, Director and member of the Executive Committee of Allen & Co., Inc , I have been involved in mergers, acquisitions, pricing of public and private sales and purchases of securities. I have also been involved in reviewing and passing on public and private financial transactions which are up for decisions with Allen & Co., Inc. I have looked at and reviewed approximately 3 situations a week for the past 13 to 14 years. These situations have run the gamut of investment opportunities and have involved origination, investigation, evaluation, negotiation, closing and monitoring.

Since 1960 I have been investing for my own and family's account in both private ventures and publicly held securities.

I am also President and Director of I. Wit Realty Corp. which has several real estate interests and a portfolio of publicly held securities. With respect to this corporation and several family trusts of which I am Trustee, I am the individual primarily responsible for making investment decisions.

BASIS OF APPRAISAL

1. MODERN MAID FOOD PRODUCTS, INC. in August and September 1968 had issued and outstanding 21,600 shares Class "A" voting common stock, 86,400 shares Class "B" non-voting common stock, and 25,200 shares 5% cumulative preferred stock Par Value $100 a share.

2. There were two gifts of 25,680 shares each on August 21, 1968, and three gifts of 8600 shares each on September 24, 1968 of Class "B" common stock of MODERN MAID FOOD PRODUCTS, INC.

3. The Class "B" common stock had no voting rights with respect to election of Directors, had no representation on Board of Directors, or any rights thereto, had no right to a voice in management or in determination of company policies or any rights thereto. Class "B" shareholders had no right to effect a change in Company's charter or by-laws to give them any such rights.

4. Holders of Class "B" common stock had no right to any dividends or other distributions unless declared by the Company's board of directors, except pro-rata liquidating dividends pari passu with Class "A" common stock and after payment of liquidating dividends on outstanding preferred stock.

5. Cash dividends paid in years prior to 1968 were less than preferred dividend requirements after the recapitalization in August 1968. No dividends have been paid on the common stock since 1967.

6. That just prior to and during the time of transfer of the Class "B" common stock, there were no serious discussions underway or agreements or understandings with respect to the sale of securities to the public, a merger, sale , liquidation or was there in the offing a dramatic change in the business by an invention, a new process, or an acquisition.

7. The Class "B" common stock subject to gift carried no rights to sell the shares to the Company or any other person had the donee so desired. There was no "buy-out" or "buy-back" agreement.

VALUATION OPINION

Based on the above my opinion is that a willing buyer of Class "B" common stock of Modern Maid Food Products, Inc. would have been willing to pay no more than $5 to $6 per share in cash in August and September 1968.

My opinion of price takes into consideration the facts that at December 31, 1967, the pro-forma book value of the Class "B" common stock was approximately $12.35 per share (and no doubt more in August 1968); and that the pro-forma earnings per share of Class "B" common stock (after allowance for pro-forma preferred stock dividends) were approximately $2.77, $4.59, $4.28 and $4.71 per share in calendar years 1964, 1965, 1966 and 1967, respectively.

In my view, the only reason for a knowledgeable purchaser to have purchased Class "B" common stock would be as a rank speculation that some day, in some way, something would happen (a possible public offering, sale or merger of the Company) to increase the value of his investment of an order of ten times, that is an ultimate realization of $10 for each $1 invested. Such an investor would have nothing else to expect from his purchase - dividends, salaries, or other compensation.

In my experience no knowledgeable buyer wants to buy a locked-in position in a private company unless he believes, there is a good possibility that within some finite period of time, three to five years or less, he will receive substantial appreciation on his investment - that is on the order of five to ten times. Usually when making such an investment, a knowledgeable buyer has some protection on the "downside" - a "put" or other buy-out right - or some assurance or agreement or well grounded opinion based on the circumstances of the company or controlling stockholders that he will be able to "realize" in the near future on his investment. Where such facts exist, a purchaser may view five times on his investment as a reasonable expectation.

In the case of Modern Maid Food Products, Inc. as I understand the facts, no such protection agreement, conditions, or assurances were present. For these reasons, I am of the opinion that the higher multiple on the spectrum of expectations, that is ten times on an investment of $5 to $6 a share would have been the only sensible one based upon 1968 price/earnings valuation of ten to twelve times 1967 pro-forma earnings per share.

This is the method that I used in 1968, and as an investing principal and advisor to others, I would have applied in considering the possible purchase of Class "B" common stock of Modern Maid Food Products, Inc., in 1968.

Ex. 18

THE AMERICAN APPRAISAL COMPANY, INC. *Standard and Poor's Building* 345 Hudson Street New York, N.Y. 10014 212/989-7780

March 22, 1974

Sidney Gelfand, Esq.
136 East 57th Street
New York, N. Y.

Dear Mr. Gelfand:

In accordance with your authorization I have appraised 77,160 Class B common shares of Modern Maid Food Products, Inc., for gift tax purposes, consisting of two blocks of 25,680 shares given as of August 21, 1968, and three blocks of 8,600 shares given as of September 24, 1968.

The appraisal was made for the purpose of expressing an opinion of the fair market value of these various stock interests as of their respective dates of transfer. The term "fair market value" as used herein is defined as the amount at which the assets would exchange between a willing buyer and a willing seller, neither being under compulsion, each having reasonable knowledge of all relevant facts, and with equity to both.

The attached report sets forth the details of my investigation and the conclusions reached.

As a result of this investigation, I have concluded that the fair market value of these stock interests as of their respective dates of transfer is Twelve Dollars ($12.00) per share.

I have made no investigation of, and assume no responsibility for, the title to, or any liabilities against, the property appraised.

Respectfully submitted,

THE AMERICAN APPRAISAL COMPANY, INC.

Gordon V. Smith
Senior Appraiser

Reviewed & Approved
C.E.O. Walker, Vice Pres.

Qualifications - Gordon V. Smith

Since joining The American Appraisal Company, Inc. in 1963, I have been continuously engaged in the valuation of a wide variety of property for a number of purposes.

The American Appraisal Company employs over 900 professional staff members and during the past several years has served nearly 300 of FORTUNE's tabulation of the 500 largest industrial corporations in the United States.

I have assisted in, and been responsible for, the execution of appraisal assignments in all parts of the United States and Canada. I am a Senior Member of the American Society of Appraisers and a member of the National Association of Accountants. I was the author of a technical paper on the use of cost indexes in the appraisal process which was published in the May 1973 issue of the Journal of the American Society of Appraisers.

During the past five years I have been personally responsible for valuation engagements including:

Valuations of capital stock or other securities for:

National Telephone Directory Corp.
Providence Body Company
Dynatech, Inc.
NCNB Corp.
Trans-Union Corp.
Raytheon Company

Four confidential engagements concerning the valuation of capital stock.

Valuations of a business enterprise involving extensive market investigations of capital stock prices.

Champion International	The Stanley Works
Mobil Chemical Co.	Stone Container Corp.
Handy & Harman	Veeder Industries
Bundy Corporation	Gould, Inc.

Other engagements relating to consultation service in the areas of taxation, accounting, and rate-making.

Questor Corp.	Pennwalt Corp.
Quaker Oats Co.	American Can Company
NL Industries	Warnaco

Purpose - The purpose of this appraisal is to develop and express an opinion of the fair market value of 77,160 Class B common shares of Modern Maid Food Products, Inc. as of August 21, and September 24, 1968 for gift tax purposes. More specifically, the ownership of the shares being appraised is divided as follows:

Given in trust August 21, 1968 for the benefit of:	
Stanley Silverman	25,680 shares
Joel Silverman	25,680 shares
Given in trust September 24, 1968 for the benefit of:	
Susan Silverman	8,600 shares
Ann Silverman	8,600 shares
Beth Silverman	8,600 shares
Total	77,160 shares

The term "fair market value" as used herein is defined as the amount at which the assets would exchange between a willing buyer and a willing seller, neither being under compulsion, each having reasonable knowledge of all relevant facts, and with equity to both.

Background - Modern Maid Food Products, Inc. was formed as a New York Corporation in 1952 as the successor to a partnership formed in 1933. The company has two wholly-owned subsidiaries, Modern Maid Food Products of Louisiana, Inc., and

Modern Maid Realty Corp., both incorporated under the laws of the State of Louisiana. The company manufactures breading and batter mixes, prepared to customers' specifications. The company also manufactures prepared flour mixes for use in restaurants, hotels, and other institutional outlets. The offices of the company are located in Garden City, New York.

On August 12, 1968, the company exchanged newly authorized Class A and Class B common stock and shares of 5% cumulative preferred stock for the then outstanding common stock. The resulting capitalization was as follows:

Class A Common Stock	21,600 shares
Class B Common Stock	86,400 shares
Cumulative Preferred Stock, 5%	25,200 shares

The Class A and Class B common stock rights were identical except that all voting rights were vested in the Class A common stock.

On August 21, 1968, Mr. Jack Silverman, Chief Executive Officer of the company and holder of the majority interest in the Class A common stock, gave in trust 25,680 Class B common shares to his son, Stanley Silverman and 25,680 Class B common shares to his son, Joel Silverman. Shortly thereafter, on September 24, 1968, Seymour Silverman established three trusts for his daughters, Susan, Ann and Beth, giving 8,600 shares of Class B common stock to

each trust. The subject valuation concerns the fair market value of these various stock interests as of the respective dates of transfer.

As part of this appraisal, I held discussions with company management to gain a familiarity with the nature and operations of the business. In addition, financial statements audited by Arthur Andersen & Co. were provided to me and have been accepted without investigation as properly reflecting business operations. These income statements for the years 1964 through 1967 and the balance sheet as of December 31, 1967 have been reproduced in this report and appear as Exhibits 1 and 2, attached.

Valuation - In any valuation of property, consideration must be given to the values indicated by the cost to replace the property, the income-producing capabilities of the property, and the price paid for comparable property in an active, public market. With respect to shares of capital stock, the valuation approach based on market value is considered to be the most appropriate.

In the course of this study, consideration has been given to the following:

1. the history of Modern Maid Products, Inc. and the nature of its business.
2. the financial condition of Modern Maid, the nature of its assets, and the book value of the stockholders' equity.
3. the historical operating results of Modern Maid.
4. the investors' appraisal of the common stock of companies in similar lines of business as evidenced by the ratio of earnings to the price of their common shares, where it is publicly traded.
5. the general economic and stock market conditions at and around August, 1968.
6. such other factors as have a bearing on the fair market value of the shares.

Where an appraisal is made of the capital shares of corporations which are publicly traded in the stock market, the valuation procedure is rather straightforward. The value, in this case, is represented in most instances by the known amount at which the shares would sell in the public market, net of selling costs and taxes. With respect to the capital

shares of Modern Maid which are being appraised, the procedure is made considerably more difficult due to the fact that the shares are closely held. The only sale of these shares was that of 4,790 shares to 19 persons in August, 1968 at a price of $10.00 per share.

In addition, the capital shares of Modern Maid are "restricted" securities that can not be distributed publicly without registration under the Securities Act of 1933. Such securities can only be acquired directly from the issuing corporation in a private placement, or from an existing holder. In either case, however, the transaction is privately negotiated and carries with it a "letter" contract to the effect that the security is being purchased as an investment and will not be re-offered for sale after a short period of time. Further, the number of buyers of a restricted security is limited to avoid being construed as a public offering, which would require registration with the Securities and Exchange Commission.

Valuation Premise - The valuation of the designated Class B common shares of Modern Maid is based on comparative analysis of prices of the capital stock of publicly traded companies in a similar business, modified by the limiting conditions,

under which these shares could be sold. These conditions arise due to the following facts:

1. Modern Maid Products, Inc. capital stock is not publicly traded.
2. The marketability of these shares is further restricted in that: (a) the prospective purchasers must be relatively few in number requiring a substantial individual investment, (b) a prospective purchaser must be willing to hold them as a long term investment with no guarantee of a future public market, (c) these shares carry no voting rights and (d) the control of the issuing corporation is in the hands of a single individual.

Valuation Technique - As a first step in the valuation an investigation was made into the economic conditions and the general atmosphere of the securities market in August-September, 1968. During 1968, the stock market, as evidenced by the Standard & Poors index, moved upward, reaching an all-time high for that time, of 108.31 (1941-1943 equals 10) in the second quarter of 1968. The price earnings ratio of

Standard & Poors index of 425 industrial stocks was 17.39 during the second quarter of 1968. In mid-August of 1968, the price earnings ratio of the Dow Jones Industrial stocks was 15.9. The price earnings ratio of Barron's 50 stocks at this time was 15.4. In mid-September, these price earnings ratios were 16.8 and 16.3, respectively. While there were forecasts of some slowdown in the economy, the general atmosphere of the securities market was generally favorably at this time.

I concluded as a result of this investigation that there was no appreciable difference in the market climate between the dates of August 21, 1968 and September 24, 1968 to warrant their separate consideration for purposes of this valuation.

Specifically, a search was made for companies in a similar business to Modern Maid and whose securities were publicly traded. The following were selected as being the most closely representative of this group:

American Bakeries Co.
Continental Baking Co.
Interstate Bakeries Corp.
General Foods Corp.
Pillsbury Co.
Quaker Oats Co.

It is recognized that these firms are very large, and enjoy diversified markets, and that these facts must be considered in any comparison with Modern Maid. The relative sizes and price to earnings ratios of these companies are as follows:

	1967 Net Sales (000,000's)	August 1968 Price/Earnings Ratio
General Foods Corp.	1,652	18
Continental Baking Co.	621	16
Quaker Oats Co.	555	19
Pillsbury Co.	526	18
American Bakeries Co.	298	13
Interstate Bakeries Co.	196	12

The net sales of Modern Maid in 1967 were $11.7 million, having grown at the rate of 6.5% during the previous three years. Further, with regard to Modern Maid, the following data was developed as of December 31, 1967:

Debt/Equity ratio	0.3
Current ratio	2.9
Quick ratio	2.6
Sales/Working capital	4.7
Sales/Accts. Receivable	4.4

This data indicates, in my opinion, that would exhibit, to a potential investor, adequate financial resources for the future growth of its business.

In determining the value of the Modern Maid equity if it were publicly traded, I have given consideration to:

1. The price/earnings ratios of the firms shown above.
2. Modern Maid's relative small size.
3. The fact that Modern Maid was a regional, non-diversified company.

I have, therefore, concluded that the equity of Modern Maid, if offered to the public market would sell at a price/earnings ratio of 10. This includes a consideration that shares of unknown companies offered to the public are often "underpriced" in order to make them attractive to the buying public and to help assure a strong after-issue market.

For Modern Maid, the earnings to which this multiple should be applied must be determined. It assumed that a potential investor in Modern Maid's securities at August 1968 would have available to him the income statements for 1964 through 1967 which have been reproduced as Exhibit 1 of this report. While the net sales of

Modern Maid for the period 1964 through 1967 exhibited a steady growth, the net income presented an unsteady pattern. For this reason, I considered it appropriate to average the income for the three years prior to the valuation:

	Net Income (ooo's)
1965	$ 622
1966	589
1967	636
Average	$ 616

On the basis of average earnings of $616,000 multiplied by the price earnings ratio of 10, it is estimated that the fair market value of the equity of Modern Maid Products, Inc. as of August 1968 was $6,160,000, assuming the securities were being traded in an active, public market.

Since these securities were not, in fact, publicly traded, an adjustment must be made for this to recognize the lack of liquidity inherent in the purchase of closely held securities.

One measure of this adjustment which has been utilized is the costs incurred by companies in offering their capital

stock to the public market. These costs include underwriting fees, commissions, legal and consulting fees, and management expenses. I have concluded that a discount of 15% would be an appropriate adjustment.

Applying this adjustment to the publicly traded value of $6,160,000 yields an adjusted value of $5,236,000. This represents the fair market value of the equity of Modern Maid with consideration of its closely held status.

As previously noted, the equity of Modern Maid Products, Inc. consisted of both preferred and common stock. The preferred stock was comprised of 25,200 shares of cumulative $100.00 par value stock with a 5% dividend. The total dividend requirement on an annual basis for these shares of preferred stock was $126,000. Considering the net income available in the previous three years, the payment of this dividend is relatively secured and the cumulative feature further protects the investor in these securities.

I then made an analysis of publicly traded issues of cumulative preferred stock with a Standard & Poors rating of BBB or BB. These issues were considered to be comparable

with the Modern Maid preferred shares if it were publicly traded and subject to such a rating. Nine such issues were analyzed and the average yield of the group was 6.4%. I have, therefore, concluded that investors in preferred stock of comparable quality to that of Modern Maid desired this level of return on their investment. Therefore, in order to obtain this level of yield, the price which would be paid would be correspondingly less than the par value and is measured by the capitalization of the stated dividend ($5.00) at the investor's rate of 6.4%, or $5.00 ÷ .064 = $78.13. I have used $80 per share, considering Modern Maid's dividend coverage of 5 times. On this basis, the indicated value of the 25,200 shares of Modern Maid preferred stock is $2,016,000.

If $5,236,000 represents the fair market value of the equity of Modern Maid, then this amount, less $2,016,000 represented by the preferred shares, or $3,220,000, remains at the value of the common shares.

The total issued and outstanding common shares of Modern Maid at August 1968 were as follows:

Class A Common	21,600	shares
Class B Common	84,400	shares
Total	108,000	share

On a per share basis, the fair market value attributed to the common shares of $3,220,000 is $29.81.

This value of $29.81 per common share represents, in my opinion, the fair market value of the Modern Maid common shares if an investor could purchase a minority interest in one clas of common stock with the typical rights with respect to voting, dividends, and capital distribution.

As we have pointed out, this is not a possibility with respect to the shares being appraised and a further adjustment must be made.

A further consideration must be made at this point of the lack of marketability of the Class B common shares being appraised due to the fact that they represent a separate class of common shares, do not have any rights for future registration, and do not carry with them the voting power to compel a future registration. As a measure of the loss of marketability due to this condition, an analysis was made

of the purchases of such securities by the Value Line Development Capital Corporation during the period of January 1 to July 23, 1968. This investment company makes a speciality of the purchase of restricted securities.

During 1968, four such investment companies were formed:

The Diebold Technology Venture Fund, Inc.
Fund of Letters, Inc.
SMC Investment Corporation
The Value Line Development Capital Corporation

Of these, only Value Line was in existence long enough to have recorded experience by August 1968.

The Value Line analysis compares the price paid for restricted securities compared with the average market price of the "free" (registered) securities of the same corporations. The data included in this study is presented as Exhibit 3, attached.

This data indicates that the purchase price of the restricted securities represented a discount ranging from a low of 16.7% to a high of 71.4% when compared with the average market price of the free securities on the date of acquisition. The average discount was 44%. A further examination indicates that one half of the securities analyzed showed discounts over 40% and that their average was 57.2%.

The reason for the discount which is exhibited in this analysis has been well stated in the following excerpts from the February 1, 1968 prospectus of the Value Line Development Capital Corporation:

> "In many cases there will, after the corporation's initial operating period, be no public market for the portfolio securities of the corporation representing investments in development situations. Accordingly, it may be difficult to sell such securities at a price representing, in the opinion of management, their fair value until such time as the issuers of such portfolio securities have developed to the point where such securities are treated in a public market."

> "Where registration is required, a considerable period may elapse between the time when a decision is made to sell the securities and the time when the corporation would be permitted to sell under an effective registration statement. During such period, if adverse market conditions develop, the corporation may not be able to obtain as favorable a price as that prevailing at the time of the decision to sell."

The prospectus of the Diebold Technology Venture Fund, Inc. issued July 12, 1968 states similarly:

> "As previously indicated, it is expected that a substantial portion of the funds' portfolio may consist of highly speculative securities with no public market or a limited public market, issued by small and unseasoned companies..... In many cases, it may take several years before portfolio securities of unseasoned companies are considered to have become sufficiently valuable and appropriate for sale. It is expected

> that a substantial portion of these securities may be purchased by the fund subject to investment representations or under other circumstances which would require registration of the securities under the Securities Act of 1933 in connection with a subsequent public sale. Such a registration may result in material delays in making a sale as well as exposure to a loss from a declining market."

In these statements, these knowledgeable investors set forth the risks which are inherent in the purchase of restricted securities of unseasoned companies, of which the Class B shares of Modern Maid are an example.

Further, after recognizing that these risks exist, these investment companies have sought to reduce this risk in a number of ways. Value Line has stated that it is a policy that at least 50% of the value of restricted securities in its portfolio must be the subject of a commitment from the issuer to register, at Value Line's request, the securities under the Securities Act of 1933. That is, the restricted securities are bought with a registration agreement as a condition of the purchase. Similarly, SMC Investment Corp. entirely limits its purchase of restricted securities to those corporations where there already exists some free stock in the public market. The Fund of Letters, Inc. states that its portfolio is mostly of restricted stocks of corporations which also have free stocks in the market. These policies of

the funds reduce the amount of risk in two ways. First, where the fund owns restricted securities of a corporation which has publicly traded shares, the fund has access to financial data on the corporation and the value of the publicly traded shares serves as a benchmark to indicate the public investor's appraisal of the company. Secondly, by providing as a condition to the purchase of restricted securities an agreement for future registration, the funds are assured that if growth in the issuing corporation takes place as expected, a public market for their shares can be utilized.

Any analysis of the discounts set forth above, then, must give consideration to the fact that they exist after consideration of the efforts of the fund to reduce the risk as discussed. With respect to the Class B common shares of Modern Maid being appraised, a prospective purchaser of these securities has absolutely no assurance that the securities would ever be subject to registration in the future, and must consider that the control over a decision to register any securities of Modern Maid rests with a single majority stockholder.

Further, since there were no publicly traded shares in existence, such an investor would likely not be able to obtain any financial and operating data on the company whose shares he owned.

A potential investor in these shares, therefore, would, in my opinion, have to be willing to invest a substantial amount (due to the restrictions on the number of possible buyers) at a greater risk of being able to capitalize on the expected growth of Modern Maid than that taken by the investment companies cited above.

After careful consideration of these facts, it is my opinion that an appropriate discount to be applied to the Class B common shares of Modern Maid Products being appraised is 60%. Applying this discount to the previously determined price per share of $29.81 yields a price per share of $11.92.

Conclusion - After consideration of the facts outlined above, and the employment of valuation techniques which, in my practical experience I consider appropriate, it is my conclusion that the fair market value of the 77,160 Class B common shares of Modern Maid Food Products, Inc. as of August 21 and September 24, 1968 is fairly stated in the amount of $12.00 per share.

Exhibit # 1

MODERN MAID FOOD PRODUCTS, INC.

and Subsidiary Corporations

Consolidated Statement of Operations

(000's)

	1964	1965	1966	1967
Net Sales	8,256	9,772	10,674	11,739
Cost of Sales	5,291	6,292	7,163	7,710
Gross profit	2,965	3,480	3,511	4,029
Selling, G & A expense	2,105	2,300	2,413	2,789
Operating income	860	1,180	1,098	1,241
Other Income (expense)	(3)	15	30	43
Income before taxes	856	1,195	1,127	1,284
Taxes	430	573	538	649
Net Income	426	622	589	636

(may not add due to rounding)

Exhibit # 2
Page # 1

MODERN MAID FOOD PRODUCTS, INC.

and Subsidiary Corporations

Consolidated Balance Sheet
December 31, 1967

(000's)

ASSETS

Current Assets		
Cash	498	
Acc'ts. Receivable	2,656	
Inventories	415	
Cert. of Deposit	150	
Interest Rec.	4	
Total Current Assets		3,724
Fixed Assets		
At Cost	2,314	
Depr. Reserve	1,039	
Net Fixed Assets		1,275
Other Assets		
Deposits	54	
Investments	26	
Cash Value-Ins.	33	
Deferred Charges	13	
Net Leasehold	4	
Total Other Assets		130
TOTAL ASSETS		5,128

LIABILITIES AND CAPITAL

Current Liabilities		
Accts. Payable	$ 744	
Taxes Withheld	25	
Accrued Expenses	238	
Fed. Income Taxes	212	
Due to Officers	22	
Notes Payable	36	
Total Current Liabilities		1,277
Capital		
Common Stock	216	
Preferred Stock	144	
Surplus	3,491	
Total Capital		3,851
TOTAL LIABILITIES		5,128

(may not add due to rounding)

THE VALUE LINE DEVELOPMENT CAPITAL CORPORATION

PURCHASES OF RESTRICTED SECURITIES

January 1 - July 23, 1968

	Acquisition Date	# Shares	Cost Per Share	Average Market Price-Free Stock	Indicated Discount
Aerological Research, Inc.	5/10/68	35,000	$ 7.00	$ 12.38	43.5 %
Clayton Corp.	7/24/68	100,000	5.25	7.81	32.8
E. L. I. Industries, Inc.	7/1/68	30,000	9.70	19.00	48.9
Jayark Corp.	4/24/68	45,450	5.50	16.25	66.2
Landa Industries, Inc.	6/10/68	75,000	3.33	7.50	55.6
Metalurgical Int'l. Inc.	4/4/68	20,000	25.00	33.00	24.2
Miles-Samuelson, Inc.	5/29/68	45,000	7.25	11.50	37.0
Process Plants, Inc.	7/23/68	25,000	30.00	50.00	40.0
Tally Corp.	5/21/68	10,000	30.00	45.25	33.7
Tintair, Inc.	4/5/68	250,000	1.00	2.38	58.0
United Utilities - Florida	7/16/68	20,000	2.50	8.75	71.4
The Valtronic Corp.	3/11/68	50,000	5.00	6.00	16.7

Exhibit #3

A75

Ex 19

APPRAISAL

MODERN MAID FOOD PRODUCTS, INC.

CLASS "B" COMMON STOCK

HERBERT S. CANNON

111 Broadway

New York, N.Y. 10006

Philips, Appel & Walden, Inc.
Member New York, American and Other Principal Stock Exchanges

111 BROADWAY · NEW YORK, NEW YORK 10006
CABLE ADDRESS - BROKERAGE
TELEX 62206

TELEPHONE
(212) 364-9000
BRANCH OFFICES
FORT LEE, NEW JERSEY
VIENNA, AUSTRIA

March 22, 1974

Mr. Sidney Gelfand
136 East 57th Street
New York, New York

Dear Mr. Gelfand:

Pursuant to your request, I have made a study of the financial and market factors affecting the fair market value of 51,360 shares of Class B (non-voting) Common Stock of Modern Maid Food Products, Inc. on August 21, 1968 and the fair market value of 25,800 shares of said stock on September [illegible] 1968.

The appraisal report details the following data:

(a) My qualifications as an appraiser of securities for market values.

(b) Nature of the stock and relevant statistical data.

(c) Valuation factors.

In my opinion, the fair market value of the Class B Common Stock of Modern Maid Food Products, Inc., subject to gifts on August 21, 1968 and September 24, 1968, was not in excess of $2.00 to $5.00 a share dependent upon the anticipated time the company would remain privately owned.

Sincerely,

Herbert S. Cannon
President

HSC/lb
enclosure

QUALIFICATIONS - HERBERT S. CANNON

EDUCATION

1949	Cheshire Academy, Cheshire, Connecticut	
1953	Washington and Jefferson College	B.A.
1960	Fordham Law School	L.L.B.
1968	Fordham Law School	J.D.
1969	Admitted to the Supreme Court of the United States	

BUSINESS HISTOFY

1962 - 1970	Weis, Voisin, Cannon & Co., Inc. and predecessor firms (Members of the New York Stock Exchange)	President and Director
1967 - 1970	Elgin National Industries, Inc. (Listed on the New York Stock Exchange)	Chairman of the Board
1971 - 1973	Cannon, Jerold & Co., Inc. (Members of the New York Stock Exchange)	Chairman of the Board and President
1970 to present	Cannon Industries, Inc.	Chairman of the Board
1971 to present	Solvent Chemical Company, Inc.	Chairman of the Board
1973 to present	Philips, Appel & Walden, Inc. (Members of the New York Stock Exchange)	President and Director

PAST DIRECTORSHIPS

The Franklin Mint	Listed on the American Stock Exchange
Bartell Media Corporation	" " " " " "
Thompson-Starrett Corp.	" " " " " "
Diversified Data Services & Sciences, Inc.	" over-the-counter
Product Applications, Inc.	" " " "
Carson Chemical Corporation	Private corporation
Data Information Services, Inc.	Listed over-the-counter
Generics Corporation of America	" " " "

CURRENT DIRECTORSHIPS AND CONSULTING ASSOCIATIONS

Decision Systems, Inc.
Electro-Catheter Corporation
Nation-Wide Check Corporation

Financial Consultant to several public corporations (Past and Current):

Bartell Media Corporation (ASE)
Briggs Leasing Corporation (OTC)
Diversified Data Services & Sciences, Inc. (OTC)
Electro-Catheter Corporation (OTC)
Elgin National Industries, Inc. (NYSE)
The Franklin Mint (ASE)
Generics Corporation of America (OTC)
Romanoff Industries, Inc. (OTC)
Royal Zenith Corporation (OTC)
Solvent Chemical Company, Inc. (Private)
Thompson-Starrett Corporation (ASE)
The Tower Fund, Inc. (OTC)
Ultimacc Systems, Inc. (OTC)

BUSINESS EXPERIENCE

I have been in charge of several finance committees of charitable organizations including the raising of capital, interim capital investment and the evaluation of operating costs and expenses.

I have served on the investment committee of The Tower Fund, Inc. which invested approximately $6,000,000.

I am a trustee of Washington and Jefferson College and a member of its finance committee which invests approximately $25,000,000.

During 1956 - 1960 I acted as an investment analyst in the evaluation of corporations for investment, merger or acquisition.

I have often served as an appraiser in the sale and merger of several public and private corporations (e.g., Rayne Industries, Incorporated, Butler Capital Corporation, Generics Corporation of America, Nation-Wide Check Corporation, Haber & Henry, Inc.) I have acted as financial consultant to Field's Baking Corporation (manufacturers of bread and bread crumbs) and to the Pechter-Field's Baking Corporation merger.

During 1962 - 1970, as President of Weis, Voisin, Cannon & Co., Inc., I was totally responsible for all financial involvements of the corporation including its syndications, negotiation of underwritings, the financial consulting department, and the corporate finance department which was instrumental in effecting a number of mergers, acquisitions and dispositions in 1967, 1968 and 1969 to the extent of:

Nature of Service	Number	Dollar Volume
Private Placements	15	$ 15,000,000
Underwritings, as Manager		100,000,000
Underwritings, as Participant		200,000,000
Mergers and/or Acquisitions		15,000,000

In 1967 I negotiated for control of the Thompson-Starrett Corporation (ASE) and became Chairman of the Board. In the three ensuing years I was instrumental in making nine acquisitions, all of which required financial evaluations of both public and private entities.

I have qualified as an expert witness in approximately seven arbitration and court proceedings requiring the evaluation of corporate worth.

NATURE OF THE STOCK AND RELEVANT STATISTICAL DATA

1. Modern Maid Food Products, Inc. was a privately owned corporation in 1968 having but three principal stockholders, one of whom owned more than 50% of the company. It was engaged in the business of manufacturing breadings and batter mixes and prepared flour mixes for sale to industrial and large commercial purchasers.

2. The Class B Common Stock of Modern Maid Food Products, Inc. was non-voting stock by the corporation's very charter and there were 86,400 shares outstanding.

3. The voting control of the corporation was lodged in the 21,600 shares of Class A Common Stock outstanding of which 12,840 shares were owned by one individual only sixty years of age.

4. Preceding the common stock were 25,200 shares of 5% cumulative preferred shares with a par value of $100 per share.

5. The book value of a common share of Modern Maid Food Products, Inc. (consolidated basis) at December 31, 1967 was $12.31 a share. Projecting 1967's earnings to August 31, 1968 on a time basis would give a book value of $15.98 a share after preferred dividends.

6. Average yearly earnings before dividend requirements in 1965, 1966 and 1967 were $615,789 and $489,789 after giving effect to the preferred dividend requirements after the recapitalization on August 12, 1968. This latter amount would be $4.53 per share on the 108,000 common shares outstanding.

7. No dividends were being paid on the common stock in 1968. Dividends paid in prior years were materially less than the preferred dividend requirements after the reorganization.

VALUATION FACTORS

1. Fair Market value is defined as the price a seller could obtain from a willing buyer having knowledge of all of the facts.

2. Modern Maid Food Products, Inc. was a privately owned corporation.

3. The Class B Common Stock was non-voting without any say in the management or control over business operations.

4. The Class B Common Stock had no marketability or immediate potential for same.

5. The type of business engaged in and the earnings multiple it might enjoy as a public vehicle.

6. The relative little growth in net earnings in the three years ended December 31, 1967 while sales increased 15%.

7. The amount of money that might be required to effect a purchase of 25,680 shares or 51,360 shares on August 21, 1968 and 8,600 shares or 25,800 shares on September 24, 1968, thus limiting the potential market.

APPROACHES

(a) A Conservative Investor may be ruled out due to the lack of liquidity, lack of dividend and the inability to have a say in management, planning, financial policies or in the possible sale or liquidation of the business.

(b) A Speculator! Due to the non-voting features of the stock and lack of market, the relative young age of management owners, the lack of incentive by management to declare dividends on the common stock (even if the corporation could afford such action), such an investor would only be interested in the possibility of a public offering some time in the future. Without a voice in management, he would be dependent upon the desires and whims of management in this respect.

A person taking such a speculative position requiring a substantial sum of money anticipates a market price profit of at least 400% within a three year period. Even if a public offering is effected, an insider's stock is usually restricted for an additional period of years from public sale.

Although underwriting conditions were good in August and September 1968, the nature of the company's business and the relative flatness of earnings in 1965, 1966 and 1967 (deviation from the mean being about 3% on the upside and 6% on the downside), this would limit the value to be placed on the company as a whole to ten times average earnings or $6,158,000. Deducting preferred stock of $2,520,000 gives a common stock potential market value of $3,638,000 or $33.70 a share if public. Since speculative investments in non-marketable closely held situations are made on the basis of a 400% paper profit, within three years, the most such an investor would pay is 20% of $33.70 or $6.75 a share. Such a price would require an investment of $173,340 from two purchasers of 25,680 shares each and $58,000 from three additional purchasers of 8,600 shares each. It would be extremely difficult to find five speculative investors with such available funds, willing to take the risk of being hung up with non-voting stock in a privately owned company with no return on investment. If only one individual were available, for such a purchase an amount in excess of $500,000 would be required, again diminishing the availability of buyers and reducing the fair market value to approximately $5.00 per share.

If a public offering or merger with a public entity could not be reasonably expected within a three year period, then I would be loathe to invest or advise any one to invest at more than a nominal amount of $2.00 per share. The amount to be invested at $5.00 a share, possibly as much as $385,000 is too significant an amount to wait upon a pure conjecture without a real possibility of liquidating one's investment.

What must be emphasized here is the purchaser of the Class B Common Stock (non-voting) without the ability to force management to change the status of the stock from non-voting common to voting common could entertain no probability of ever liquidating the stock in the public market. Due

to different class status, none of the rules of the S.E.C. or NASD permit an automatic registration, even after a substantial holding period, to enable even piece meal liquidation into the public market. This factor alone would greatly depreciate the fair market value of the stock by 70% even where underwritings are being considered.

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STOCK VALUATION

MODERN MAID PRODUCTS, INC.

1968

ESTABLISHED 1899

THE MANUFACTURERS' APPRAISAL COMPANY

Atlanta
Boston
Baltimore
Chicago
Cincinnati

Executive Offices
ROBINSON BUILDING
15th & CHESTNUT STREETS
PHILADELPHIA, PA. 19102

Cleveland
Detroit
New York
Philadelphia
St. Louis

Philadelphia, Pa.
March 14, 1974

Internal Revenue Service, Regional Counsel
26 Federal Plaza,
New York, New York 10007

Gentlemen:-

We are pleased to submit our appraisal of certain Class B Common Stock of Modern Maid Products, Inc.. It is our considered opinion that the Fair Market Value of the Stock, constituting a minority interest and as of various dates in August, September and December 1968, is best expressed as $25 per share.

Our engagement has been confined to a determination of the value of the Stock in accordance with our agreement. We have not investigated title to the property, nor the possible existence of liens, mortgages and assessments and, therefore, do not assume responsibility with respect to ownership.

Neither the employment to make, nor the compensation for the appraisal is contingent upon values reported. To the best of our knowledge or belief, all statements and information contained in this report are true and correct, and no important facts have knowingly been withheld. The Manufacturers' Appraisal Company has no present, prospective, direct or indirect interest in the property herein appraised.

This analysis was made by the use of methods and procedures conforming to ethical standards of practice.

Respectfully submitted,

THE MANUFACTURERS' APPRAISAL COMPANY,

Vice President.

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PURPOSE OF APPRAISAL

The purpose of this appraisal is to estimate the Fair Market Value of certain Class B Common Stock of Modern Maid Products, Inc. as of various dates in August, September and December, 1968. The concluded values will consider the fact that the subject shares constituted only a minority interest in the subject company, that the stock was non-voting, and that there was no ready market for it.

DEFINITION OF FAIR MARKET VALUE

Fair Market Value is defined as the price expressed in terms of money which the subject stock will bring in a normal market, allowing a reasonable time to find a purchaser who buys with full knowledge of the subject company's advantages and disadvantages, with neither party being under compulsion to buy or sell.

The valuation of privately-held corporate stock, stock for which their is neither an established market price nor even a ready market, presents certain difficulties. Analysis of the subject stock poses several interesting valuation problems. First,the valuation dates are over five years in the past, making direct examination of the company's physical assets inappropriate, and necessitating analysis of data on an historical basis.

Second, the subject stock, although it represents an intrinsic share or part of Modern Maid Products, Inc., is both non-voting and a minority interest. Accordingly, once the total value of the subject company is determined, care must be taken to correctly apportion that total to the different classes of stock, with proper consideration of discounts in value for lack of marketability, lack of control, etc..

Third, there were few publicly-held companies which were truly comparable to the subject. Ultimately our comparisons included five companies which overlapped in some areas with Modern Maid Products, Inc., but which were dissimilar in other areas.

Fourth , one or more of the subsequent appraisal approaches to valuation must include some estimate of the future or "projected" profits of the company. The risks of reaching incorrect conclusions in these circumstances can be reduced if there is some historical basis for the expectations upon which the projections rest; and they may even be reduced considerably if quantitative historical data exists which points consistently to the same answers. If, for example a given historical progression of numbers was 70, 80, 90, 100 and 110, and the circumstances

surrounding the progression remains unchanged, it could be predicted with a degree of certitude that the most likely next number in the progression would be 120. In the case of the subject company, however, no such obvious progression exists, and the degree of certitude with which projections can be made is most certainly reduced from that of the first example. It is not however, reduced to the point of being unmeasurable, and if in fact it must be estimated in order to complete certain appraisal approaches, it can best be accomplished by a thorough examination of historical trends.

Finally, a number of appraisal techniques must be established which will provide an effective measure of the total value of the company. At the onset of this study a number of approaches to valuation were considered. Ultimately this number was reduced to three: 1 - Return on Net Worth Approach, 2 - Price-Earnings Ratio Approach, and 3 - Comparable Public Enterprise Approach.

VALUATION

RETURN ON NET WORTH APPROACH

This approach considers a normal return to the balance sheet net worth of the company. Excess return may be capitalized at a higher (intangible) rate of return and the resultant value added to the net worth to provide an indication of total company value. Inasmuch as the book net worth figure is likely to be understated, this approach will generally produce a lower limit of value. Examine the following summary:

Net Worth (12/31/67)	$3,921,320
Normal Return (At 13%)	509,772
Actual Return	620,406
Excess Return	$110,634
Capitalized at 15%	$737,600
Total Indicated Value	$4,658,920
(Rounded)	$4,659,000

Company	Net Worth	Return	% Return
Martha White Foods, Inc.	$8,281,012	$1,451,583	17.53
Manischewitz (B) Co.	3,690,017	255,963	6.94
Bridgeford Foods Corp.	2,179,105	263,838	12.11
Sap's Foods, Inc.	1,150,343	181,227	15.75
Spaulding Bakeries, Inc.	2,798,349	339,180	12.12
Total/Composite	$18,098,826	$2,491,791	13.77%
Average	-	-	12.89%

Thus a rounded normal industry return of 13% is applied against the subject company's 12/31/67 book net worth of $3,921,320. The result, $509,772 is subtracted from the actual earnings of $620,406 to indicate those earnings related to assets, other than those included in net worth. Capitalizing the $110,634 on excess return at a 15% rate of return produces $737,600 in value to those assets other than those included in net worth, and a total value including net worth of $4,659,000 (rounded).

RETURN ON NET WORTH APPROACH--CONTD.

These figures are based upon financial information that was approximately nine months old at the time of the gifts of subject stock. Assuming in September 1968 some reasonable knowledge of current earnings, and net worth produces a considerably higher total value. Utilizing rounded earnings of $700,000 and net assets of $4,200,000($817,917.77 and $4,399,330.84 respectively were actually reported in 12/31/68 statements) produces the following indication of value:

Net Worth	$4,200,000
Normal Return (At 13%)	546,000
Actual Return	700,000
Excess Return	$154,000
Capitalized at 15%	1,026,667
Total Indicated Value	$5,226,667
(Rounded)	$5,200,000

Thus consideration of more current earnings and net worth information produces a total rounded indication of subject company value of:

$5,200,000

PRICE-EARNINGS RATIO APPROACH

This approach compares the earnings of the subject company to earnings of publicly-held enterprises having a determinable total value through the price of their stock. It was not possible to find companies which were completely comparable to the subject. However, those companies ultimately used for comparative purposes are similar in that they are involved in making and/or sale of baked products or convenience mixers and batters. Detailed information relating to these comparable companies is contained in the addenda to this report.

Examine the following summary:

Company	Total Value	Earnings	P.E. Ratio
Martha White Foods	$30,986,888	$1,451,583	21.3
Manischewitz (B) Co.	2,918,960	255,963	11.4
Bridgeford Foods Corp.	5,250,838	263,838	19.9
Sap's Foods, Inc.	2,052,288	181,227	11.3
Spaulding Bakeries Inc.	3,467,640	339,180	10.2
Totals/Composite	$44,676,614	$2,491,791	17.9
Average			14.8
Average w/o High and Low			14.2

Thus these five publicly-held enterprises indicate that a multiplier of 14 conservatively reflects the average relationship between earnings and price. Applying this to the subject company's earnings for the year ending December 31, 1967 ($620,406) produces a total value of $8,685,684.

This approach thus far has considered the use of publicly-owned companies whose securities possess good, or reasonably good, listed or quoted markets. The subject company's securities, on the other hand, are closely-held by a relatively few stockholders, and there is no listed or quoted

PRICE-EARNINGS RATIO APPROACH--CONTD.

market for them. The value of these securities has, so far, been determined just as if such a market existed. Adjustment thus should be made for this factor.

While the amount of this adjustment could perhaps, be determined on a "judgment" basis, it is our opinion that the most realistic method of measuring this negative element of value is to ascertain what the actual cost would be to create a public market for the securities. Since such a public market would normally be created by a public offering of the securities through investment bankers or brokers, the problem becomes one of determining the costs of such flotation.

Comprehensive data on the costs of public flotation of common stocks were compiled with respect to issues registered with it by Securities and Exchange Commission. This data is summarized as follows:

Size of Flotations (Millions of Dollars)	Number of Flotations	Cost of Flotation as a Percent of Gross Proceeds
Under - 0.5	4	19.69%
0.5 - 0.9	15	13.68%
1.0 - 1.9	25	12.48%
2.0 - 4.9	30	8.61%
5.0 - 9.9	9	6.38%
10.0 - 19.9	5	4.88%
20.0 - 49.9	2	5.48%

It will be seen that flotations have been grouped in accordance with the size of flotation. In the right-hand column is shown the cost of flotation expressed as a percentage of gross proceeds of the flotation to the company. It will be noted that, as the size of the flotation increases, the cost of flotation as a percentage of gross proceeds declines.

PRICE-EARNINGS RATIO APPROACH--CONTD.

Thus the cost of the subject flotation would be an estimated 6% - 8%. Utilizing 8% as a reasonable amount needed to make the subject stock truly marketable produces a rounded indication of total value of:

$7,990,000

COMPARABLE PUBLIC ENTERPRISE APPROACH

This approach is based upon the concept that the total value of the Subject Company may be ascertained through comparisons with similar public enterprises which, through the price of their stock, have a determinable total value.

Investors consider many factors in deciding what price to pay for a given stock. Three very important items are: earnings, net worth and sales; and comparisons between the comparable companies and the subject company on these basis will provide a meaningful approach to value. Ultimately five public companies were selected as the basis for comparison, and they are summarized in the addendum to this report. Examine the summary on the following page.

Thus the earnings, net worth and sales of the comparable companies are expressed as percentages of total value, averaged, and expressed as multipliers. Weighting the contributory importance of these factors to consider earnings most important and sales least important produces the following formula to value:

Value = 6.74 x earnings + .50 x net worth + .07 x sales.

Inserting the subject company data into the formula produces the following results:

Value = 6.74 x $700,000 + .50 x $4,000,000 + .07 x $13,000,000
= $4,718,000 + $2,000,000 + $910,000
= $7,628,000

Reducing this by the percentage (8%) needed to make this stock marketable, produces a total rounded value of:

$7,000,000

COMPARABLE PUBLIC

Year Ending	Company	No. of Common Shares	Average Price	Total Value
6/1/63	Martha White Foods, Inc.	1,101,756	28 1/8	$30,986,888
7/31/63	Manischewitz (B) Co.	53,072	55	2,918,960
11/1/63	Bridgeford Foods Corp.	600,101	8¾*	5,250,838
5/31/63	Sap's Foods, Inc.	256,536	8	2,052,288
12/23/63	Spaulding Bakeries, Inc.	420,320	8¼	3,467,640
	Total/Composite Data			$44,676,614
	Average Data			
	Indicated Average Multipliers			
	Weighted Equally (÷ 3)			
	Weighted (3-2-1)			
	Subject Data			
	Total			
	Less Discount for Lack of Marketability (At 8%)			
	Net Value (Rounded)			

*Offered 12/19/63

ENTERPRISE APPROACH

Earnings	Net Worth	Sales	Earnings As a % of Total Value	Net Worth As a % of Total Value	Sales As a % of Total Value
$1,451,583	$8,231,012	$4[illegible],060,353	4.68	26.73	12[illegible].29
255,063	3,600,017	9,786,494	8.77	126.40	335.25
263,838	2,179,105	10,090,474	5.02	41.50	192.16
181,227	1,150,343	5,431,515	3.83	56.05	264.66
330,180	2,798,349	10,904,022	9.78	80.70	314.46
$ 2,491,791	$18,958,826	$76,363,358	5.57	40.50	170.92
			7.42	66.20	247.16
			13.47	1.51	.40
			4.49	.50	.13
			6.74	.50	.07
			$700,000	$4,000,000	$13,000,000
			$4,718,000	$2,000,000	$910,000
					$7,628,000
					610,000
					$7,018,000
					$7,000,000

3143 [illegible] 1,69[illegible]

CORRELATION AND CONCLUSION OF VALUE

Thus the approaches considered have provided the following indications of value:

Return on Net Worth	-	$5,200,000
Price-Earnings Ratio Approach	-	$7,990,000
Comparable Public Enterprise Approach	-	$7,000,000

Each of the three approaches possesses merit but none could be considered any more than a tool to the final Fair Market Value of all of the company's stock. Elements of value are contained in each of the methods used, but a conclusion of value can be made only after weighing the worth of each approach and using good sound judgment in the determination of final values.

The Capitalization of Excess Earnings on Net Worth offers evidence of total value. However, it is limited in that the data used is gathered compositely from different enterprises, each of which use different accounting principles and techniques, different rates of depreciation, etc., causing significant variation on expression of net worth. This approach tends also to express the understatement of fixed asset value as intangible value, which it is not, thereby producing minimal values.

The Price-Earnings Ratio Approach offers evidence of total value. It too has its limitations in that the data used is gathered compositely from different enterprises using different accounting techniques, different rates of depreciation, etc., causing variation on expression of earnings. Additionally, the total company value for the five comparable companies was developed by multiplying the total number of shares outstanding times the

CORRELATION AND CONCLUSION OF VALUE--CONTD.

average price per share for the year. If the stock were subject to large fluctuations in price, the results could be significantly distorted.

The Comparable Public Enterprise Approach also offers evidence of total value, and has the same limitations mentioned for the two preceding approaches. Since, however, it weights more than one factor, it is somewhat more likely to produce a reasonable estimate of value. Accordingly, it is our considered opinion that the total value of the subject company's stock is best estimated as $7,000,000.

Thus far we have considered only the total value of the subject company. We must still estimate the approximate per share value of the subject stock, which is a minority interest and Class B(non-voting). The capital stock outstanding as of the gift dates was as follows:

Class A Common Stock	-	21,600 Shares (par $10)
Class B Common Stock	-	91,190 Shares (par $10)
Preferred Stock	-	25,200 Shares (par $100)

The preferred stock was 5% cumulative non-voting stock, and redeemable at its $100 par value. Reducing the total value of the company by the value of the preferred stock ($2,520,000) provides an indication of $4,480,000 in value to all the common stock. Consideration of an equal value of all the shares of both Class A and Class B common stock(112,790) produces a per share value of approximately $40. Discounts for minority interests can vary from 10% to 50%. It is our considered opinion that 25% best reflects the proper discount to be applied to the value of the minority interest. A summary of court cases and a study of two-step acquisitions is presented within the Addendum of this report as substantiation for the discount. Application, of this 25% discount to the $40 per share value produces a value of the shares of stock of $30.

CORRELATION AND CONCLUSION OF VALUE--CONTD.

Whether or not the subject shares should be further reduced in value due to their being Class B(non-voting) is problematical. The element missing in non-voting stock is the same as is missing in a minority interest, namely - control. Inasmuch as we have already discounted the value of the to reflect a lack of control, it may be inappropriate to further reduce the value for the fact that it is non-voting. Nevertheless, in order to make some distinction between the two classes of stock, we feel that a further reduction in value of $5 per share is reasonable, and that the value of the subject shares of stock, being Class B (non-voting), constituting a minority interest is best expressed as:

$25 per Share

ADDENDUM

A104

THE MANUFACTURERS' APPRAISAL COMPANY
Executive Offices
ROBINSON BUILDING
15th & CHESTNUT STS.
PHILADELPHIA, PA. 19102
215 568 – 6739

ESTABLISHED
1899

OFFICES IN
PRINCIPAL
CITIES

EX. 3

APPRAISAL QUALIFICATIONS

of

Hugh A. MacMullan, III

Appraisal Experience:

(A) Currently employed as a Vice-President and field appraiser by The Manufacturers' Appraisal Company, a national organization founded in 1899. Initially employed to complete real estate valuations, making valuations of intangible assets including stock in closely-held corporations since 1968.

(B) Appraisal assistant to independent appraiser and real estate broker.

(C) Self-employed for three years in construction and renovation of residential and commercial real estate; with specific experience in preparing cost estimates and engineering breakdowns.

Formal Education:

(A) A.B. degree from University of Pennsylvania, 1961.

(B) Courses in the following:

(1) Urban Renewal - University of Pennsylvania.
(2) Real Estate Brokers and Salesmen - Delaware County Board of Realtors.
(3) Real Estate Analysis - Temple University School of Business.
(4) Real Estate Law - Temple University School of Business.
(5) Property Management - Temple University School of Business.
(6) Real Estate Valuation - Temple University School of Business.
(7) Real Estate Practice - Temple University School of Business.
(8) Real Estate Finance - Temple University School of Business.

Specific Qualifications:

(A) Qualified by written examination to use the designation of "Member, American Society of Appraisers", with listed specialty of intangible assets, including stock in closely-held corporations.

(B) Found qualified to present evidence in numerous courts, informal hearings, boards of review, arbitration sessions, etc..

Specific Qualifications--contd.

(C) Qualified for Real Estate Salesman's License by written examination in the Commonwealth of Pennsylvania.

(D) Prepared Fair Market Value appraisals for buyers or sellers of property where sale was contingent upon appraisal values.

(E) Prepared other Fair Market Value appraisals that were used and accepted by lending institutions for mortgage loan purposes.

(F) Qualified by written examination as an appraiser for the State of New York.

(G) Have appraised closely-held corporations, leasehold equities, good will, franchises, license agreements, covenants not to compete, patents, trademarks, copyrights, contracts, and other intangible assets.

(H) Made or participated in over 300 appraisals in 31 states. Some of the better known clients served include:

A O Industries
AMF Inc.
Addressograph Multigraph Corporation
The Anaconda Company
Milton Bradley
W. Atlee Burpee Co.
Capital Cities Broadcasting Co.
Falstaff Brewing Corp.
Hoechst Fibers, Inc.
INSILCO
The Internal Revenue Service
Keene Corporation
Lavino Shipping Co.
McGraw-Hill Co.
Mite Corp.
National Industries
PPG Industries, Inc.
Textron
Time-Life, Inc.
Triangle Industries

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COMPARABLE PUBLIC ENTERPRISE DATA

MARTHA WHITE FOODS, INC.

History: Incorporated in Tennessee May 31, 1946, name changed to Martha White Mills, Inc. in 1952, and to Martha White Inc. 1967, present title adopted September 26, 1967.

Business: Co. manufactures or processes and distributes convenience mixes, family flour, corn meal, baking mixes, edible dried beans and mixed feed in the southeastern U.S.. Co. also distributes convenience foods nation wide.

Consolidated Income Account, years ended:

	June 1,'68	June 3,'67
Net sales	$40,060,853	$38,290,379
Other Income	28,888	29,048
Total	40,089,741	38,319.427
Cost of sales	27,659,414	27,368,257
Selling, etc., exp.	8,930,137	7,701,837
Depreciation	460,442	451,465
Interest	66,073	98,564
Income Taxes	1,451,583	1,224,756
Net income	1,522,092	1,474,547
Prev. earn. surp.	5,434,366	4,198,539
Dividends (cash)	321,355	238,720
Earned surplus	(1)6,635,103	5,434,366
Earn. com. share	$1.38	(2)$2.01
No. of com. shares	1,101,756	(2)734,504

(1)$4,468,927 not restricted. (2)$1.34 on 1,101,756 shs. adj. for 3-for-2 stk. split 10/68

Consolidated Balance Sheet, as of:

Assets:	June 1,'68	June 3,'67
Cash	$1,521,554	$1,980,170
U.S. Treas. bills	1,242,032	... ...
Receivables	1,869,621	1,999,634
(2)Inventories	3,572,926	3,610,877
Prepayments	36,205	31,440
Total current	$8,242,338	$7,622,121
(1)Plant, eq., etc.	2,623,769	2,670,788
Land	102,452	102,452
Construction	271,675	2,088
Trademarks, etc.	19,005	19,005
Other assets	173,697	162,307
Total	$11,432,936	$10,578,761

MARTHA WHITE FOODS, INC.--CONTD.

Consolidated Balance Sheet--contd.

Liabilities:	June 1, '69	June 3, '67
Notes, etc., pay.	$121,000	$157,000
Accts. payable	717,532	689,112
Accruals	430,554	440,998
Income Taxes	782,838	990,375
Total current	$2,051,924	$2,277,485
Long term debt-	1,100,000	1,221,000
Common stk. ($1)	1,101,756	734,504
Capital surplus-	544,153	911,405
Earned surplus	6,635,103	5,434,367
Total	$11,432,936	$10,578,761
Net current assets	$6,190,414	$5,344,636
Net tang. com. sh.	$7.50	(3)$9.61

(2)Lower cost(fifo) or mkt. (3)$6.41 adj. for stk. split.

MANISCHEWITZ (B.) CO.

History: Incorporated in Ohio, May 15, 1914. Company founded in 1888

Business: Company makes matzos(un-leavened bread), matzo meal and farfel, cake meal, Tam Tam crackers, borscht, gefilte fish, baby foods and canned soups. It also distributes pickles, canned fruits, candies other kosher grocery items, including Kosher sacramental wine.

Consolidated Income Account, years ended July 31:

	1969	1968
Net Sales	$9,801,280	$9,786,494
Royalty income	409,656	357,934
Total	10,210,936	10,144,428
Cost of sales, etc.	7,705,232	7,760,347
Selling, etc., exp.	1,888,032	1,895,680
(1)Oper. profit	617,672	488,401
Oth. income, net	59,896	60,456
Total income	677,568	548,857
Interest	121,720	111,894
Income taxes	245,000	181,000
Extraord. charge	(3)50,000	... ...
Net income	260,848	255,963
Prev. earn. surp.	3,318,211	3,168,368
Common divs.	106,120	106,120
Earned surplus	(2)3,472,939	3,318,211
Earn. com. share	(4)$4.91	$4.82
No. of com. shares	53,072	53,072

(1)After $161,763(1968, $160,339) depr. & amort. (2)$385,000 not restricted. (3) Prov. for loss liquid. of inv. in & adv. to 50% owned Canad. Co, (4)$5.85 before extraord. charge.

Consolidated Balance Sheet, as of July 31:

Assets:	1969	1968
Cash	$399,289	$349,082
Short-term inv.	... ...	395,399
Receivables, net	1,591,041	1,128,566
(3)Inventories	1,787,537	1,706,834
Total current	$3,777,867	$3,579,881
(1)Net prop., etc.	1,352,856	1,233,033
Other assets	476,579	450,966
Intangibles	144,644	164,753
Deferred charges	75,578	78,567
Total	$5,827,524	$5,507,200

MANISCHEWITZ (B.) CO.--CONTD.

Consolidated Balance Sheet, as of July 31--contd.

Liabilities:	1969	1968
Accts., etc. pay.- - - - - - - - -	$668,101	$495,822
Debt due - - - - - - - - - - - -	81,000	81,000
Income taxes - - - - - - - - - -	232,178	157,861
Total current - - - - - - - - -	$981,279	$734,683
Long term debt - - - - - - - - -	1,001,500	1,082,500
(2) Common stock - - - - - - - -	371,506	371,506
Donated surplus- - - - - - - - -	300	300
Earned surplus - - - - - - - - -	3,472,939	3,318,211
Total - - - - - - - - - - - - -	$5,827,524	$5,507,200
Net current assets - - - - - - -	$2,796,588	$2,845,198
Net tang. com. sh. - - - - - - -	$69.72	$66.42
(1) Depr. & amort. - - - - - - -	$1,790,476	$1,674,536

(2) 53,072 no par shs. (3)Lower cost or mkt.

BRIDGFORD FOODS CORP.

History: Incorporated in Calif. on Dec. 31, 1952.

Business: Business consists primarily of the manufacture and wholesale distribution of processed meats and other delicatessen foods. The sale of fresh, frozen and smoked meats and the manufacture and sale of frozen bread dough products and other miscellaneous items.

Consolidated Income Account, yrs. ended:

	Oct. 31,'69	Nov. 1,'68
Sales	$13,208,326	$10,090.474
Cost of Sales	10,603,073	7,987,345
Sell. etc. exp.	1,996,367	1,434,804
Depreciation	228,257	188,487
Fed. inc. tax	188,000	216,000
Net income	192,629	263,838
Prev. retain. earn.	482,302	313,982
Dividends	135,650	95,518
Retain. earn. 11-1	539,281	482,302
Earn. com. share	$0.28	$0.44
No. of com. shs.	704,301	600,101

Consolidated Balance Sheet, as of:

Assets:	Oct. 31,'69	Nov. 1,'68
Cash	$422,979	$180,400
Receivables	702,296	470,862
(2)Inventories	706,325	510,343
Prepayments	104,357	50,818
Total current	$1,935,957	$1,212,423
(1)Net property	1,479,150	1,026,146
Total	$3,415,107	$2,238,569
Liabilities:		
Accts. etc., pay.	$888,052	$646,008
Fed. inc. tax	70,396	165,717
Notes payable	50,000	... ...
Total current	$1,008,448	$811,725
Notes payable	121,554	... ...
Future inc. tax	106,000	78,000
Capital stk.($1)	704,301	600,101
Capital surplus	935,523	266,441
Retained earnings	539,281	482,302
Total	$3,415,107	$2,238,569
Net current assets	$927,509	$400,698
Net tang. com. sh.	$3.10	$2.24

SAP'S FOODS, INC.

History: Incorporated in Indiana June 1, 1955 as Sap's Bakery, Inc., succeeding to business founded in 1946. Present name adopted in March 1969.

Business: Engaged primarily in the production and sale of a variety of bakery products. Principal markets are supermarkets, institutions, restaurants and vending machine operators. In addition, Co. operates 3 restaurants through subsidiaries.

Consolidated Income Account, yrs. ended May 31(SEC report):

	1969	1968	1967
Net Sales- - - - - - - -	$6,762,266	$5,431,515	$4,760,539
Cost & exps. - - - - - -	6,127,184	4,967,943	4,395,998
Depr. & amort. - - - - -	166,152	134,983	129,652
Interest - - - - - - - -	33,497	25,350	25,290
Inc. taxes - - - - - - -	201,170	122,012	83,382
Minority int.- - - - - -	3,048	... ...	... ...
Net income - - - - - - -	231,215	181,227	126,217
Earn., com. sh.- - - - -	$0.90	$0.71	$0.49
On 256,538 shs. outstg.			

Consolidated Balance Sheet, as of May 31, 1969 (SEC report):

Assets	
Cash - - - - - - - - - -	$101,869
Receivables- - - - - - -	404,857
Inventories- - - - - - -	208,329
Prepayments- - - - - - -	109,986
Total current - - - -	$825,041
Net prop., etc.- - - - -	1,750,242
Other assets - - - - - -	96,284
Total - - - - - - - - -	$2,671,567
Liabilities:	
Notes, etc., pay.- - - -	$161,192
Accts., etc., pay. - - -	593,868
Fed. inc. tax- - - - - -	144,399
Total current - - - -	$899,459
Notes payable- - - - - -	$506,360
Def. Fed. inc. tax - - -	97,353
Minority interest- - - -	18,052
(1)Com. stk. - - - - - -	332,560
Retained earnings- - - -	817,783
Total - - - - - - - - -	$2,671,567
Net current assets - - -	d$74,418

SPAULDING BAKERIES, INC.

History: Incorporated in N. Y. August 16, 1926.

Business: Operates bakery selling bread, rolls and krullers in N. Y., Conn. and Pa. under name County Squire.

Income Account, yrs. ended:

	Dec. 27,'69	Dec. 28,'68
Sales, etc.- - - - - - - - -	$10,796,167	$10,904,022
Cost of Sales- - - - - - -	6,071,326	6,097,757
Sell., etc. exp. - - - - - -	3,966,249	4,026,198
Interest - - - - - - - - -	48,357	50,351
Income taxes - - - - - - -	387,832	390,536
(1)Net income- - - - - - -	322,403	339,180
Prev. retain. earn.- - - -	1,747,549	2,626,935
Dividends- - - - - - - - -	218,566	218,566
Retained earnings- - - - -	1,851,386	1,747,549
Earn., com. share- - - - -	$0.77	$0.81
No. of com. shs. - - - - -	420,320	420,320

(1)After $264,895(1968 $249,900) deprec.

Assets: Balance Sheet as of:	Dec. 27,'69	Dec. 28,'68
Cash & equity	$123,398	$260,076
U.S. Treas. bills- - - - -	780,645	544,947
Receivables net- - - - - -	467,264	406,470
(2)Inventories - - - - - -	257,257	226,643
Prepayments- - - - - - - -	154,479	153,196
Total current - - - - -	$1,783,043	$1,591,332
(1)Prop., etc., net- - - -	2,635,298	2,782,224
Cash val. life ins.- - - -	48,454	61,181
Mkt. secur., cost- - - - -	4,425	4,525
Other assets - - - - - - -	49,809	61,875
Total - - - - - - - - - -	$4,521,029	$4,501,137
Liabilities:		
Accts., etc. pay.- - - - -	$481,342	$514,829
Accruals - - - - - - - - -	27,302	18,732
Dividends pay. - - - - - -	92,470	92,470
Income taxes - - - - - - -	66,685	40,645
Other curr. liab.- - - - -	17,847	18,361
Total current - - - - -	$685,646	$685,037
Long term debt - - - - - -	752,900	837,600
Def. inc. taxes- - - - - -	180,297	180,151
Capital surplus- - - - - -	1,050,800	1,050,800
Retained earnings- - - - -	1,851,386	1,747,549
Total - - - - - - - - - -	$4,621,029	$4,501,137
Net current assets - - - -	$1,097,397	$906,295

(2)Lower of cost (fifo) or mkt. (3) 420,320 no par shs.

COURT CASES

Case No. 9. *Drybrough v. United States*[12]

Issue: Substantial discounts from fair market value of real estate holdings allowed for minority interests

Purpose of Valuation: Gift tax

Valuation Claimed by Petitioner	*Claimed by IRS*	*Final Adjudication*
$134,328	$526,800	$171,452

Supplementary Information: Parcel of real estate and four closely held realty corporations holding six parcels of real estate, four parking lots, and two smaller pieces of property

Issues Argued

Although there were other issues involved, the principal one was the valuation of gifts made in May and June 1957, by Mr. and Mrs. F. W. Drybrough to their son. The gifts consisted of an undivided 40% interest in real estate located in Louisville, Kentucky, and 40% of the issued and outstanding capital stock of four real estate holding corporations. The parties agreed that the value of the underlying realty comprising the sole assets of the corporations must be determined and the mortgage indebtedness, if any, should be deducted therefrom, and that 40% of the resulting figure is the "book value" of 40% of issued and outstanding capital stock of the individual corporations. Both sides produced qualified experts and filed briefs summarizing their valuations. The gross valuations of the underlying properties (before deducting mortgage indebtedness of $749,000) of the respective parties and the court were as follows:

	Plaintiff	Defendant	Court
Parcel of land	$ 238,750	$ 238,653	$ 238,000
Properties held by corporations	1,006,400	1,314,220	1,142,000
Total	$1,245,150	$1,553,073	$1,380,800

[12] 208 F. Supp. 279 (W.D. Ky. 1962).

The next and important issue was what discounts, if any, were to be applied to the undivided interest in real estate, and to the minority interests in the corporations. The government contended that no discounts should be allowed, whereas the witnesses for the taxpayer testified to the contrary. They testified that a discount ranging up to 40% should be allowed on the undivided interest in the parcel of land. One witness for the taxpayer testified that a holder of minority interests in Kentucky corporations cannot control policy, dividends, or liquidation, and therefore such interests are not readily marketable. He suggested a discount on the "fair market" value of the 40% interest in the corporations ranging from 33⅓% to 50%. A witness for the government proposed a discount of "approximately 20%."

Decision

From a consideration of all the testimony the court concluded that the value of the undivided interest in the unincorporated real estate should be discounted 15%, and the minority interests in the corporation 35%.

Case No. 19. *Inga Bardahl*[22]

Issue: Low valuation approved for minority interest, based on discounts for lack of marketability and one-man management

Purpose of Valuation: Gift tax

Valuation Claimed by Petitioner	*Claimed by IRS*	*Final Adjudication*
$286,000	$400,400	$256,000

[22] 24 T.C.M. 841 (1965).

Supplementary Information: Bardahl Manufacturing Corporation—manufacturer and marketer of oil and grease additives

Issues Argued

Ole Bardahl and his wife Inga Bardahl made gifts of Bardahl stock aggregating 2,860 shares to their daughters and grandchildren in 1959. In gift tax returns filed they valued such shares at $100 each. As of December 30, 1959, immediately prior to the gift here involved, there were 20,000 shares of Bardahl stock outstanding, over 85% of which was owned by Ole Bardahl.

The Commissioner, in his notice of deficiency, determined that the fair market value of the Bardahl stock transferred by gift was $140 per share.

Testimony developed that all of Bardahl's operations were under the direct personal supervision of Ole Bardahl, including manufacturing, marketing research, sales, and contacts with distributors.

The petitioners produced an expert witness who valued the Bardahl stock at $68.615 per share. The government's witness, a valuation specialist with the Internal Revenue Service, valued the stock at $132 per share. Incidentally, the book value per share of the stock was $96.57 on December 30, 1959.

Decision

The court found that there were insufficient sales of Bardahl stock to establish its value. Both the petitioner's and the government's experts relied on the price–earnings ratio of two competitor corporations whose stock was publicly traded. The ratio thus derived was applied to the weighted average per-share earnings of Bardahl for the five years ending with the year of gift discounted by the government's expert by 20% for the cost of floating a stock issue to the public and 10% because Bardahl is a "low diversification manufacturer, its products being related in nature and usage, which fact increases the vulnerability to competition and creates a sensitivity to savings in the business cycle." The petitioner's expert used the same 30% discount and "assigned an additional 20 per cent discount because of the one-man management of the corporation and the minority interest being valued."

The court felt that the government's expert should also have discounted his value for "the one-man management of the corporation" and the fact that a prospective buyer would consider anticipated earnings, particularly since available data indicated a decline from the high point achieved for the year of gift.

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TWO STEP ACQUISITIONS

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	Initial Date	Price	Percent Acquired
IPL Corp. - U.S. Consumer Prod.	12/65	$5,000,000	50%
LTV Electrosystems - Mercor Inc.	1/67	1,500,000	33%
General Aniline & Film Corp. - Ruberoid Co.	5/67	33,300,000	26%
Pennzoil Co. - United Gas Corp.	12/65	225,600,000	42%
Glen Allen Corp. - Phillip Carey Mfg. Co.	2/66	11,300,000	23%
U. S. Smelting, Ref. & Min. Co. - Mueller Brass Co.	3/66	20,300,000	62%
Diebold Inc. - Lamson Corp.	6/66	7,300,000	90%
Philadelphia & Reading Corp.- Lone Star Steel Co.	8/65	64,300,000	73%

TWO STEP ACQUISITIONS

50

(discounts for minority interests)

Approximate Price for 100%	Subsequent Date	Price	Percent Acquired	Price For each 1%	Minority Interest Implied Discount
			41		
$100,000	5/66	$3,200,000	4%	$78,050	22%
45,500	4/67	5,900,000	67%	88,100	97%
1,150,000	5/67	90,000,000	74%	1,220,000	6%
9,370,000	1/68	618,000,000	59%	10,660,000	90%
423,000	6/67	37,800,000	72%	525,000	25%
240,000	9/66	3,700,000	13%	205,000	17%
66,700	7/66	600,000	10%	60,000	31%
877,000	4/66	17,900,000	27%	660,000	24%
				Ave.	31%
				Ave. w/o High-low	24%

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UNITED STATES TAX COURT

SEYMOUR SILVERMAN, ET AL
Petitioner

vs

COMMISSIONER OF INTERNAL REVENUE
Respondent

DOCKET NO. 3707-72
3708-72
3709-72
3710-72

LOCATION OF HEARING: NEW YORK, NEW YORK

DATE: March 27, 1974

BEFORE: THE HONORABLE WILLIAM H. QUEALY

APPEARANCES:

SIDNEY GELFAND
WALLACE MUSOFF
for Petitioners

STANLEY J. GOLDBERG
for Respondent

The $17 a share alluded to by counsel is when there was only 2,000 shares common stock -- I think even less than 2,000 shares of common stock outstanding and there was no -- 25,200 of preferred requiring 126,000. In other words the $17 might have been 34,000 or 28,000 or 17,000 dollar dividend. Subsequently, we have requirements on the preferred stock of 126,000 and there were no dividends then on the common. Just as background, Your Honor.

Mr. Jack Silverman, will you take the stand.

THE CLERK: Raise your right hand. Do you solemnly swear that the testimony you are about to give in this case to be the truth, the whole truth and nothing but the truth, so help you God?

THE WITNESS: I do.

THE CLERK: Please be seated. State your full name and address for the record.

THE WITNESS: Jack Silverman, 847 Ivy Hill Road, Woodmere, New York.

J A C K S I L V E R M A N, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. [illegible]:

Q Mr. Silverman what was your position in Modern Maid Food Products Inc. in 1968?

A I was the President of the Corporation.

Q And your position today?

A The same.

Q It has been stipulated there was a recapitalization of Modern Maid Food Products Inc. in 1968. What was the purpose for that recapitalization?

A We are in a highly competitive business and the thought occurred to those in administration to solidify the employment of key employees. And for that reason we thought it advisable to offer a, a sale of stock, non-voting, and a -- also an intent on our part to have these people retain a small interest in the corporation.

Q Were you or the people who owned the stock at that time also interested in receiving a fixed return on part of your investment before the employees were to receive anything?

MR. GOLDBERG: Objection, Your Honor, that's a leading question.

THE COURT: Restate your question.

MR. GELFAND: All right.

BY MR. GELFAND: (Resuming)

Q Were there any other reasons pertaining to, uh, the receipt of a fixed -- to receipt -- were there any other reasons why the reorganization took place -- recapitalization took place?

A Well we -- I personally wanted to insure my fixed

investment and at the same time offer the employees who were with us a interest in the business but certainly not to have any ultimate say in the running of the operation.

Q When did you first advise the employees, the corporation was going to offer them an opportunity to buy stock in the company?

A After we received word that the recapitalization would take place and we thought we would offer them the stock when it would be a non-taxable -- or the stock would not be subject to tax.

Q We have stipulated the corporation sold the total of 4,790 shares Class B common stock at $10 a share to 17 persons. How was this figure of $10 a share determined?

A I thought it was a fair value based upon the book value of the company and the fact that there were no dividends, it was a good return, ultimately.

Q When did you decide to make -- no, pardon me -- did you consider or intend the Class B common stock sold by the corporation at $10 a share to be in the nature of compensation?

A No.

Q Did the corporation claim any deduction on its income tax return as compensation or otherwise for any possible excess value of the stock over $10 a share?

A No.

Q Will you please describe the nature of the business of Modern Maid Food Products in 1968.

A Modern Maid Food Products is categoried as a food processor. We have two divisions, one of which is manufacture of prepared flour mixes for baking purposes, which is known as the Food Service Division. The second division is that of the Food Processing Division where we manufacture, the terminology is breading and batter mixes sold to frozen food processors.

Q Would you please --

A The Food Service Division distrib -- manufactures and distributes its products to eating places, ultimately. The Food Processing Division ultimately distributes its product to frozen food processors.

Q Will you please explain what you mean by a prepared flour mix.

A A prepared flour mix is one that is made from a base of all raw materials in dry form to which only water would be added for baking purposes.

Q Who are your competitors in the prepared flour -- Who are competitors of Modern Maid in the prepared flour mix field?

A It can be categoried as Pillsbury Flour Mills, and General Mills, D.C.A. Food Industries, they are the major ones.

Q Was there -- Who are your competitors in the breading and batter mixes?

A In that category we have Newly Wed Baking Co. of Chicago, we have D.C.A. Food Industries, and also the Griffith Laboratories of Toronto, Canada.

Q D.C.A. Industries, was that previously known under any other name?

A It was known as Donut Corporation of America.

Q Was there any agreement attached to the Class B Common Stock that was the subject of gift to buy the shares back if so requested? That is, the Class B stock that was subject to your gift, was there any agreement for the company to buy that back if -- or for you to buy it back, if requested?

A None that I recall with the possible exception of if employment terminated, or upon death.

Q You don't know whether there was any agreement or not?

A I doubt -- I doubt if there was.

Q Did the Class B Common Stock have any right by agreement or otherwise to have representation on the Board of Directors, or a voice in the management, business policy, or dividend declaration?

A No.

Q Up to and including the date of your gifts of the Class B Common Stock of Modern Maid Food Products Inc., were there any negotiations or agreement for the public sale of any securities for the merger or sale of Modern Maid Food Products, Inc.?

A No.

Q Up to and including the time of the gifts, did you have any intention for Modern Maid Food Products Inc. to become a public owned corporation, or to merge or sell said corporation?

A No, there was not.

Q During the summe. of 1968, did Modern Maid Food Product -- was there any impending dramatic change in the operation of Modern Maid Food Products Inc. as the result of any invention, new products -- new process or acquisition?

A No.

Q One moment please. Mr. Silverman, Modern Maid Food Products Inc. did go public in October 1969, 14 months later.

A Correct.

Q When did you have your first negotiations with the underwriters or any underwriters in connection with that public offering?

A It was in March of 1969.

Q All right. Will you please explain to the Court

what -- how that arose and what occasioned it?

A Well the year 1968, the latter part of 1968 saw an expansion in our business. We were looking for new fields to conquer so to speak because our present facilities were running to capacity. We were looking for a plant to be built either in the Midwest or possibly in Canada. Canada became very attracted to us at that time because we had the opportunity of purchasing a flour mill in Streetsville, Ontario. That mill was known as Reid Milling Company. The approach was made to us by their President, Mr. Paul Helliwell, to possibly negotiate the purchase of the mill or else put up a plant for breading and batter mixes right along side their operation in Streetsville, Ontario. That gave us the thought of the need of a -- increased capitalization or increased monies should be -- have to put up one or two more plants because the demand for our product was growing nationwide and we found it difficult to fulfill it -- fulfill the demand with the current facilities we had at that time.

Q How did that -- when then -- how did that lead to the discussion of going public?

A Well, my son Stanley, who was in conversation with friends of his and others, discussed our problem and the thought was given to him and he brought it back to me in early '69 of why don't we look into the possibility of going public. He had spoken to somebody and this party

brought him together with, ultimately, the underwriter.

Q Excuse me one moment, Your Honor.

(pause)

Q Mr. Silverman, could you identify this book please.

A These are the minutes of our Board of Directors meetings, of Modern Maid Food Products.

Q All right. I turn your attention to the minutes of Dec -- the 6th day of December 1968, particularly with regard to the bottom paragraph -- oh yes -- May I have this marked for identification.

** THE CLERK: Petitioner's Exhibit 15 marked for identification.

BY MR. GELFAND: (Resuming)

Q Does Exhibit 15 for identification refresh your recollection when you had these discussions with reference to Reid Milling in Canada?

A Yes, this has reference to our discussion and the Board of Director meeting so indicate. Can I read it?

Q Not yet. Is this the time that you had the discussions that led to the requirement for the fund for going public?

A This was about the time we presented it to the Board of Directors and a decision made to seek other plants for activity and ultimately seek a public issue for the needed funds.

MR. GELFAND: I offer this page in evidence. I want to make a photocopy of it.

MR. GOLDBERG: Respondent has no objection to this Your Honor.

** THE COURT: It will be received.

(Whereupon, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 15 was received in evidence, as described above.)

MR. GELFAND: Your Honor, may I retain this --

THE COURT: You may substi--e --

MR. GELFAND: And then substitute a photocopy.

BY MR. GELFAND: (Resuming)

Q Mr. Silverman, will you now read this para -- last paragraph on the page of the minutes of December the 6th, 1968.

A A discussion followed as to the plans for expansion into the Canadian area and particularly with respect to the serious talks underway with Reid Milling Limited. It was pointed out that the Corporation may be required to make a substantial investment, since the operation in Streetsville, Ontario Province of Canada, will involve the construction of a building and the necessary equipment for a breading operation.

In view of the heavy expenditures involved in the modernization of the existing plant, it may become necessary to arrange some financing before proceeding with the Canadian proposal. In any event, all problems associated with it are being checked out and there will be shortly -- there shortly will be a conference in New York with the representatives of Reid Milling Limited to move this matter. The Directors authorize Jack Silverman as President to enter into such preliminary agreements as he may deem necessary for the purpose of concluding this project.

Q Thank you.

MR. GELFAND: No further questions, Your Honor.

CROSS EXAMINATION

BY MR. GOLDBERG:

Q Mr. Silverman, would you say your company was a --

THE REPORTER: Would you stand --

MR. GOLDBERG: Is this one working?

BY MR. GOLDBERG: (Resuming)

Q Mr. Silverman, would you categorize your company as an expansion minded one?

A Today it is.

Q Or even in 1967 and 1968?

A In '68 it became one, yes.

Q Had your sales and profits substantially increased over the last 4 or 5 years prior to 1968?

received in evidence, as described above.)

MR. GOLDBERG: Thank you very much, Your Honor. The respondent will substitute copies of this.

BY MR. GOLDBERG: (Resuming)

Q Mr. Silverman, back in 1968, in June, when you had your first recapitalization and you created the B shares of common stock, you testified that one of the purposes was to solidify the employment of certain key employees. Is that correct?

A Right.

Q And you sold approximately 4,700 I believe you stipulated --

A 4,790

Q 4,790 shares of this B stock to both employees and, I see in the stipulation, also to Arthur Jaspan and Joseph Jaspan. Could you tell me who these two people are?

A They were our counsel, company counsel.

Q Did you also execute a buy, buy-back agreement with them also?

A Yes.

Q Why was there a need to create approximately 91,000 shares of B stock, non-voting stock, when you -- when you only sold approximately 5,000 to, to these people we've stipulated to, either employees or your counsel?

A The 17 or 18 people who were involved were -- the stock was sold to these individuals for the prime purpose of ensuring their employ and relationship with our company; it had nothing to do with the 91,000 shares you referred to.

Q Did you intend to make large gifts of stock to your children at the time?

A At that time, we did.

Q And, uh, is Seymour Silverman your brother?

A He is my brother.

Q Do you know at the time he also made substantial gifts to his children?

A That's right.

Q Why didn't you have any buy-back agreement executed between the trustees for your children and yourself, like you did for the other 49 or 4,790 shares of stock?

A At that time one of my children was not in our employ and it was a gift to my children ultimately if they should carry on the business.

Q So you intended them to have a, an ownership interest in the business?

A Ultimately, yes.

Q Ultimately. Why must -- Have you bought back any of the 4,790 shares of stock to date?

A No. No.

Q Did your company pay dividends on the B stock, or

67, wanting to buy this company?

THE WITNESS: Yes, sir. We've had many approaches from larger companies to purchase our or acquire our company.

THE COURT: Seapack or Ocean Products, or Booth Fisheries, any of those?

THE WITNESS: Booth Fisheries subsequently was taken over by Consolidated Foods and although many inquiries were made, we thought it not desirable to sell to a customer who would find it difficult to maintain their status in the field. But many other larger companies have made approaches to purchase ours. We listened but never entertained any ultimate decision because we wanted --

THE COURT: Well, was any offer ever made to you?

THE WITNESS: No, not directly by way of net dollars and cents.

THE COURT: In other words, you never got to the -- got to the stage of how much? --

THE WITNESS: That is right.

THE COURT: Anyone would be willing to pay for the company?

THE WITNESS: No, never.

THE COURT: Thank you, Mr. Gelfand.

MR. GELFAND: Thank you, Your Honor.

REDIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Silverman, were you interested in selling your business, or you were interested in preserving it for your sons?

A I was interested in preserving it for my sons and I still am.

Q Uh, when the possible need for additional funds arose in late '68, early '69, in connection with Reid Milling, was it -- was the first thought of going public or did that subsequently come out? In other words, were you interested in financing or were you interested in going public?

A We are always of the opinion that whatever expansion was necessary in our business we could do it from internally, but when it came to a point of putting up a new plant, we thought not to use our own funds and to go to a public issue, as was suggested by -- to my son that it was the wiser thing to do.

Q Did you look for the public issue, or was this suggested to him as a possibility?

A It was suggested to him in conversation with one of his friends who ultimately suggested he go to see a certain underwriter.

Q Prior to the time your son, Stanley, brought the idea of going public, what type of financing were you contemplating?

A We weren't seeking any outside financing. We, we

didn't contemplate any financing, excepting if we had to build a plant, we thought of going to a banking institution. But the advice submitted to us was not to go that direction.

Q You talked about expansion of your business in 1968, do you recall whether that took place in the early part '68 and the latter part of '68, apparently your conversations with Reid Milling you said took part in the latter part of '68 --

A That is right.

Q By the latter part, maybe I can refresh your recollection -- Can you tell me what this is Mr. Silverman?

A This is a reply as --

Q No, just what is it?

A This is a Reid Milling letter to us based on a visit we made in Canada --

MR. GELFAND: May I have this marked for identification?

** THE CLERK: Petitioner's Exhibit 16 marked for identification.

BY MR. GELFAND: (Resuming)

Q What is the date of this letter?

A October 26th, 1968.

Q All right. Does that recall to you when you first had your first conversation with them or conference with them?

A It was shortly before then that we spoke on the telephone, that was Mr. Helliwell and myself, and then we

arranged for this visit in Canada.

Q And the date of this visit in Canada was October 26th, 1968?

A The date of the visit was, I think, October 14th, two days prior.

Q Two days prior. All right.

MR. GELFAND: I'd like to submit this in evidence please.

MR. GOLDBERG: I have no objection, Your Honor.

THE COURT: It will be received.

(Whereuppn, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 16 was received in evidence, as described above.)

BY MR. GELFAND: (Resuming)

Q Mr. Silverman, after December 31st, '67, were there any financial statements prepared for you up to the time of the gifts that you made? In other words we have a financial statement of December 31st, '67?

A Right.

Q Did you receive -- were there interim audits, interim financial statements, or did you get them just once a year? Shaking your head doesn't say anything.

A I'm sorry. No, there were none prepared that I

know of.

Q All right.

A Excepting the Annual Report which was December 31st.

MR. GELFAND: I have no further questions, Your Honor.

RECORSS EXAMINATION

BY MR. GOLDBERG:

Q Just two very brief questions. Mr. Silverman, if the price is right would you have sold your company?

A I can say that by saying any price, anything is for sale at a good price.

Q I see.

A The question is, what was the right price?

Q What would you sell your company for?

A I can't answer that right now.

Q But you would be willing to sell it, if the price was right?

A There'a a price for anything. I say, yes, it could be sold, but I can't tell you now what I would get for it.

Q Uh, I believe there's a letter in evidence back in October --

MR. GELFAND: He has it, the last exhibit.

MR. GOLDBERG: The last exhibit.

BY MR. GOLDBERG: (Resuming)

Q Dated October 26, 1968, from Reid Milling, -- how did you learn about Reid Milling and their -- in this deal?

A I mentioned earlier that in that period, or prior to then, there was a telephone strike in Canada and I recall distinctly that -- I'm sorry, there was a mail strike, a mail strike in Canada, and Mr. Helliwell called me on the telephone indicating that he would want to get in touch with us, but mail being so slow and he indicated that he would call on the phone to see if we were interested in a joint venture. I told him a joint venture at that time would not be what we were looking for, but we would be glad to speak with him, perhaps to either buy his mill or put up a plant near his mill. That ultimately led to the first visit in the latter part of October 1968.

Q How were you two people brought together? Was there a broker?

A Just by -- no.

Q Just by word of mouth or by --

A Just by, call it coincidence, he just called us on the telephone and it opened our thinking that we should perhaps entertain a proposition of that kind, inasmuch as one of our major competitors, as I listed earlier, Griffith Laboratories, had a plant in Canada.

Q Have you done any business with Reid Milling prior to this time?

A Never.

Q Have you -- did you hear of their reputation?

A I ultimately sought it out and found out what their reputation was.

Q Fine. So it was sometime prior to prior to October of 1968 that you --

A It was the early part of October, or during the middle of October that I sought it out.

MR. GOLDBERG: That's all, Your Honor.

FURTHER REDIRECT EXAMINATION

BY MR. GELFAND:

Q This telephone call that -- was that an unsolicited telephone call?

A Unsolicited.

MR. GELFAND: I have no further questions, Your Honor.

THE COURT: You may be excused, Mr. Silverman. Thank you.

THE WITNESS: Thank you.

MR. GELFAND: Mr. Witt.

MR. GOLDBERG: Your Honor, could we have a 5 minute recess.

THE COURT: All right, we'll have a 5 minute recess.

THE CLERK: Rise please.

(Whereupon the hearing in the above recessed at 11:20 a.m., as described above.)

THE CLERK: Would you spell your last name please.

THE WITNESS: (spelling) W-I-T).

H A R O L D M. W I T, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Wit, we have stipulated to your qualifications and business experience and I'm not going to ask you any questions with reference thereto. But could you summarize briefly the basis of your appraisal report. How you look A and evaluate shares of common stock of a company, similar to the Class B stock of Modern Maid Food Products Inc. and how you arrived at the value you have?

A I'd to say that I, I, -- I don't think the way -- if I -- the question is the way that, that I think about it. I -- As I said I'm with an investment banking firm and, you know, I am -- I am a principle and so that they way I would look at this would be, I think, the way I would look at it, you know, as a buyer at that time. And supposedly a willing and knowledgeable buyer. And as, as I understand the facts that the stock we're talking about, the Class B stock --

Q Pardon me, do you want a copy of your report in front of you?

A No.

Q You don't need it?

A No.

Q All right.

A That the Class B stock, as I understand it, -- in the first place the company was a private company then and the Class B common stock had no right, the holders had no right to vote for the election of Directors; had no right to notice of meeting; had no right to, to change the relevant corporate documents to give them such a right; they had no contract giving them any right to elect a Director of the corporation; they had no right, as I understand it, except informally to influence the business of the corporation in any way; and they had -- so they had no right to elect Directors; they had no right, as I understand it, the Class B stock to, to receive dividends by any charter document, except as I understand it, liquidating dividends pari passu with the Class A stock in the event of liquidation after payment of the, of the, of the Class, of the preferred stock dividend. As I understand the facts, that they preferred stock requirements after the so-called reclassification of 1968 were, whatever they were, were much greater than the combined total for dividends paid, both the preferred and common, prior to that date. And also, as I understand it, that after the recapitalization in 1968, no dividends were in fact paid on the common stock at any time.

Also, as I understand it, the, the -- at the time that we're talking about, or just prior to the time, there were no serious discussions, contracts that would indicate that the company was, was considering a public offering of its securities, or private sale of its securities to a, that's a third party buyer, such as any institution. There were no discussions or contracts relating to a possible sale of the company, a possible major purchase by the company of a major asset, or liquidation of the company.

As I also understand it, that at that time, there were no what I call no things going on that would have changed in a fundamental and radical way, or a very, you know, important way, the business of the company, either by entering into a new field that promised hopefully greater earnings of a new invention, or a new process that would in the view of someone like myself offer the prospect of a serious change in the dimension and the type of a business.

I also understand that, that somewhere in here, that. that -- that there were no Class B stock that that's under discussion here, there were no buy out or buy back arrangements, in other words there was no put arrangement by, by contract or by understanding with respect to that Class B stock.

And those of the, the, you know, the facts that would have come to me as a principle or as a possible advisor to

others, as to whether or not to buy stock like this.

Now, it would seem to me -- and also I understand -- I've been through the figures and I understand that at the time we're talking about, I guess in December of 1967, that the stated book value was something like $12.35 a share and undoubtedly was greater at the time, you know, when the gifts were made because the company was earning money.

And also, I understand from the figures in the prospectus and other things I've looked at that, that the, the average earnings, depending on how you play this game, different people look in different ways, were after preferred dividend on a pro forma basis which is the way you, you adjust these things, that if you take the 3 or 4 years prior you're talking about and average earnings, you know, of $4 a share, so that my own view of what I might pay for it, that is not more than $5 or $6 a share at the time, takes these things into account. It doesn't take into account the sort of things you'd have to have much more information about, which would be the quality of the earnings, you know, the, the actual assets on the balance sheet, you know, how you would view those, whether they were in fact stated properly and how you would discount them. But I don't really believe that for the sort of thinking that I've been trained to do about value that those things are particularly relevant.

So that I concluded in looking at it and based upon my way of looking at things and experience I have had that you'd have to take a look at this situation, it's a completely locked-up situation. I mean, with absolutely no right of a buyer of Class B stock to have anything to say about the business of the company, to change his condition in any way, to demand a public offering of stock, in any way to -- he'd have to be completely passive and hope that some day in some way that something would happen, either through a sale or a liquidation or a public offering, to give him some value to his stock. And I would say that, that a man who was a knowledgeable person and a experienced investor, that is one who, who sees a number of different things and who not only anticipates in investing that he's going to hopefully make some big gains but obviously take some losses along the way and also be locked up along the way, since we're talking here at the price that I think, you know, is a price that makes sense of I guess with even the smallest block of stock that was, that was given away, you know, $30, $40,000, given my prices, and the biggest block, the $125 - $130,000. That he would, in this situation, look to making ten times on his money and that would be what he would be looking for now, in this situation if he was looking for that, and taking those $4 earnings and taking the, the excessive valuations which Your Honor has stated, were given at the time, that he

would say, okay, here's a company that's earning $4 a share average, maybe it'll earn a little more and maybe it'll earn a little less, it's a good earnings record but, no know, not you know it's not startling like IBM or Polaroid or one of those things. That, okay, let's say that we go public sometime maybe and if the prevailing conditions are, which they were around 1968 for companies like this, you know 10 times, 12 times. Let's say we're talking about 12 times $4 or 4 and a fraction, we're talking about $48, no $50, maybe 10 times 5 is, you know, 50, perhaps $5 is a good number. $6. I mean, we're talking here, I think, about a way of thinking that is not subject to fine, statistical analysis. It's not subject to fine appraisal methods. It's a sort of thinking of what I might hope to get if all things worked out the way they might. And if the market conditions remain more or less the same and in a situation where I've absolutely nothing to say that will either make my investment liquid or give me something else that will compensate me for locking up my money, such as dividends, salary, and so forth. And I would say that, that as a professional investor that if there were other conditions that based upon, you know, my judgement of the people or the pressures on the business or financial pressures on the stockholders that would have said okay even though I don't have a contract, and even though I don't have an understanding, there's so much pressure on the

business that they've got to go public, sell out, or do something where I can see that my investment will become liquid. And in that case, I might have said, well I'm alright maybe, 6 times on what I've put in, or 5 times what I've put in, is a reasonable expectation. But certainly not, under the conditions, that, that seem to be present here which is a completely locked up situation with, with a company that with all due respects was, you know, a good company but a company that I'm sure was in a cut-throat competitive industry where I'm sure there were sales relationships, and no matter how much I investigated it, I couldn't find out what they were, about competitive situations which I'm sure, you know, I probably woulnd't have taken the time to do because of the, you know, amount of money involved. And that's generally the sort of thinking I would do, or would have done at that time considering what I thought this thing might have been worth.

Q Thank you, Mr. Wit. In addition to your own views as to how you would have invested, is that the way you were also advising others? I mean in situations that were coming--

A Well, I, I don't -- the, the -- My experience has been with a firm where we, it's not always the case, but, but in most instances we're the principles ourselves. And we're -- because of my employment relationship that, that we as

employees of the firm, if we bring in something, we expect to put our own money in it.

Q Pardon me, I misunderstood what -- When you said you, you for Allen and Company.

A No when I say I'm an employee of that firm that if, if, if a deal comes in that I am involved in, that is originated, work it up, if the firm or its associates in the firm put in money, I'm expected to put up my own, so that as a principle I think, you know, very carefully about, you know, it's my own money. I'm not just sitting there collecting the fee and you know smiling when the thing goes down drain; get another customer. It's my own money. It's the firm's money. And I've also, you know, had friends in deals and so forth. I've also had experience in pricing public deals and have been through the whole, I think, range, you know, investment possibility.

Q Were there actually deals made during these period of years on the basis you have just explained?

A Well, I'm sure -- Yeah, there were and, and certainly that mode of thinking about, you know, of trying to, and it's not very precise, of trying to, sort of discount risk which we're really talking about. Certainly I've done a lot of those. I've just sort of, I mean they're different types of things. There's nothing let's say exactly on point, but-- but the -- we've been in deals where we put money into compan-

ies that, that were locked up, you know, that had earnings, that had certain features about them. But I'd say that in each of those situations, and that's why this is sort of different and it's a hard thing for me to even put a value on, because I, you know, in each of those things, there was something involved in the deal, either formally or informally, that gave us the feeling that within a relatively short time, there would be liquidity produced either by, by reason of the, of the formal commitment, by reason of the, of the financial requirements of the business, or by reason of, of the temperament of the principles or the controlling people involved in the deal.

Q In other words, the valuation of $5 to $6 a share that you have in your report, that does presuppose going public or becoming liquid at some time?

A Well, I would say that, that -- I don't say presupposes going public. I'd say a man who has a, looks a lot, you know, has a lot of different investments, might say, well, you know, this looks like an interesting business: this looks like good people; you know, they have good earnings; there's a book value there; well, I'll put some money in it and, you know, maybe some day in some way, you know, something will happen; in the meantime, I can afford to sit there without any return or salary.

Q But when you say liquidity, you're referring to

a merger or a sale out of the business.

A Well. I'm -- liqudity I'm referring to something where somebody -- where, where at some point I can turn in this stock certificate for, for dollars. That's why I mean by liquidity.

Q Mr. Wit is this the report that you have prepared?

A It's my illegible signature.

Q And this sets forth the basis on which you arrived at your figure of $5 to $6 a share?

A Yes, sir.

MR. GELFAND: Your Honor, may I -- I'd like to submit, but I think we ought to mark the original in evidence.

** THE CLERK: Petitioner's exhibit 17 marked for identification.

** THE COURT: Petitioner's Exhibit 17 will be received.

(Whereupon, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 17 was received in evidence, as described above.)

THE COURT: Let me ask you, Mr. Wit, can you conceive of any circumstances under which you would recommend the purchase of this Class B stock at any price, unless there was something -- that you could get your hands on that would

indicate that at some stage of the game, why there would be a market in which you could resell it?

THE WITNESS: Well, I'd say, Your Honor, that depends a little bit on the time that we're thinking about. I think that, that if we're talking about the period of 19, you know, '64 or '65, 6, 7, 8, and perhaps into '69, that my view would be perhaps a little different than it is today because of the changed market conditions. And I would say that, that, you know, there might be a type of person around that time, and given the facts about that time, there were so many deals going on, so many mergers, so many sales, so many, you know, that a man, you know, with -- looking at something like this might say, well, no matter what they say, you know there is that possibility that that will happen. And consequently if I had sufficient money and didn't have to use, you know, that money for groceries that, you know, I'd say why not take a shot, you know, I mean, that cliche that we all use. But perhaps -- and, and now of course with, with the public underwriting market, you know, and the stock market changed so much, you know, probably wouldn't touch it with a ten foot pole. But at that time, you know, the, the atmosphere was different.

THE COURT: Can you account for the fact that a year later, and I don't think the market conditions were any better in '69 -- as a matter of fact, isn't it true that by

1969, the, the zest with which people expected to buy un, unseasoned securities and make fortunes had, had abated a little bit?

THE WITNESS: I'd say --

THE COURT: They'd been a few burned by then,hadn't there?

THE WITNESS: A few burned, but none killed and, and it had abated but it was like, you know, sort of like the last throes of fever, you know, there were still a few highs back and forth. And I don't think people really believed at that time, I mean, you know, that's my -- that it was all over. There was still, you know, these -- no one believes that such easy times aren't going to last forever.

THE COURT: Can you account for the, the ability of Ladenburg to market this stock at what amounted to an equivalent of about $75 a share?

THE WITNESS: Well, I mean without trying to be disrespectful to my profession, it's not really a profession but art, I, I don't really know, you know, who there customers were, or enough about there syndicate operation to be able to answer that in any, in any way. I, I do remember at that time that if one had a business that was -- that was -- that looked solid where it looked like they had a history of good earnings that, you know, what most underwriters would do, would say, you know, 10 or 12 times earnings and that

was sort of like the cliche of the time. And buyers unfortunately, you know, didn't really, you know, look carefully into the business and didn't make the proper comparisons and didn't do the hard thinking. If they had made money with a broker and the broker called them up and said, gee I've got this great thing coming out here and why don't you buy 300 shares and the man would probably say yes.

THE COURT: Was this about the time Nathan's came out do you recall?

THE WITNESS: I don't recall.

THE COURT: Mr. Goldberg.

MR. GOLDBERG: Yes, sir.

CROSS EXAMINATION

BY MR. GOLDBERG:

Q Mr. Wit, in your report you stated that, I refer you to page 4, that someone who would've invested in this company would have won an increase of, of about 10 times on his investment, in other words 10 -- $10 for every $1 he's invested.

A That would have been his expectation.

Q Oh, his expectations. How many people in the market really were able to meet their expectations?

A We're, we're not talking about the market. What we're talking about, as I understand it, is the state of mind of someone who is a willing buyer under those sets of

facts and what, what, what I as, as a person, you know, who was a principle with some experience would look to say if everything works out what would be -- what I would hope to get from this and then discount that back. Now, I think when I say a willing buyer, I'm talking about somebody who also knows enough to know that if he puts other money in things like this he's also going to lose it, all of it sometime. And I've put money in, you know, maybe about 15 to 20, you know, different types of deals and, you know, there've been several bankruptcies and several things haven't worked out, so when you're looking at this you're not just saying I expect to get all my investments this way. But if I do them all and I'm in a high risk business and if I average down then maybe if I'm lucky, I can average out, you know, maybe 2 times my money over a period of 3 years. That's what I'm really talking about. I'm not saying that --

Q In other words this, this was -- this is your advice for someone that would be investing?

A What is that, sir?

Q That you would want realization of 10 times --

A I would say --

Q Or 1000 %?

A Yes, sir. Yes, sir. Under the circumstances that I --

Q Over how many a year period would you expect this?

A Well it's not mathematical because and, and, you know, I think if you're experienced in the investing business you know that everything always turns out wrong and that your timing is always wrong and that the things you expect don't happen, things you don't expect, happen. So that you can't be very precise. You look at these things and say, gee if it all works out maybe I'll make -- uh, put in 10 and get out 50. But I know that in the world it doesn't work out that way and maybe three other things I put my money in I lose it or make 2 times or, you know, make 1 time and get it back after 5 years. So I'd say it's sort of an averaging.

Q So in other words, an investor would be very happy to get 25% return every year, or growth on his investment?

A I think we're talking about different things. I think that we're about here a different type of investing than the man who goes into the stock market where he has liquidity. I mean, liquidity to me is a vital, vital element here. And if a man goes into the stock market, I mean they used to say a few years ago that the best investors would look to get 20% compounded on his money before taxes. And that was, you know, fabulous, you know, investing if a man could do that. But here I think we're talking about a different dimension of investing. We're not, we're not talking about buying stocks on the market, we're talking about a private, locked-up, you know, position that doesn't have

liquidity, that doesn't have dividends, that doesn't have, you know, any way that the man can get his money out, aside from going to the principle and holding a gun up to his head.

Q Did you have -- what resource data did you have when you made your report? Did you --

A What, who?

Q Resource data?

A What's that mean?

Q Oh, financial data, statistical data, anything, I mean how did you --

A I don't think the financial data means a damn thing in this sort of thing. Excuse me.

Q Did you speak to Mr. Silverman at all?

A No, sir.

Q Would you say this was a particular -- was this a growth company?

A Well I'd say it, it, it was a company that, that's why I said in, in the conditions of, of looking at it that it didn't seem to me from looking at the prospectus and, and the facts I knew that there was anything at the time that would show a dramatic increase in the earnings or the possible earnings of the business. In other words, if they had had for example a new patented method of, of -- I don't know what they could do here, but -- I'll say reducing the bulk of shipping, so that they could save 30% on the shipping

rates and kill all the competition, that would have been something that would have been existing at the time that would have made, in my view, the earnings seem less relevant. And maybe if they had a new invention that I would've said well, well heck the earnings don't really make any difference and, therefore, the price, you don't have to relate as much to a hypothetical price earnings ratio, which you're going to capitalize and then figure out backwards, you know, what your dollar of investment might be worth if this, this, this might happen.

Q You consider this a solid, solid company, don't you?

A Not paricularly.

Q You don't consider a growth of between, of over 4 years of 46 cents to 83 cents a share an interesting growth pattern?

A Well, no, no, -- I -- I do, but I don't -- I didn't mean to, you know, any disrespect to Mr. Silverman and his associates, but this is not Quaker Oats and this is not Pillsbury Flour, this is one man, you know, in a family business over in Brooklyn sort of beating his brains out trying to increase his sales every year and it's not, I would say, in the spectrum of investment possibilities -- what I would call a, a -- since I'm being -- a quality company.

Q Well does General Motors double their sales in

four years?

A Sir?

Q Would a company like General Motors double their sales in four years?

A Well we're talking again about, I think, quality, earnings and growth. I'm not trying to be -- I agree the earnings did go up and therefore someone looking at it might have had a, a expectation of increasing earnings. But as I say, that, that I haven't, you know, didn't go in deeply into the quality of the earnings in that sense. How many customers there were, how much it cost to get in the business, what the competition might be, whether Pillsbury if they, you know, blew their nose could blow these fellows out of the, you know, out of the dock. I don't know.

Q How are new issues generally coming out at this time, in 1968? Were a lot of new issues issued --

A They were coming out like minnows flowing out of the stream, sir.

Q Right, and some were selling at 30, 40 times earnings?

A It was -- I'd say that was so, yes.

Q And it was a very bullish stock market then, wasn't it?

A Everyone looked like the here after was with us.

Q Do you know what the, when the, the high was reached

on the Dow Jones average?

A No, sir. I'm not -- that's not my business.

Q Oh, would be surprised if the higher was reached in December of '68 with 179 --

A I really -- whatever you say, sir --

MR. GELFAND: Your Honor -- Your Honor, I move that we strike that. I mean Mr. Goldberg is not testifying.

THE COURT: He's asking a question.

MR. GOLDBERG: -- Mr. ah.-- Mr. Wit's in the stock market, in the investment --

THE WITNESS: No, no, no I'd like to explain, I'm, I'm not -- we, we do not, I don't -- except insofar as I run some family trusts in a family business. I'm I'm not -- I don't advise people to buy a hundred shares of General Motors or 200 shares of American Telephone for their mothers. I mean that's not the business I'm in.

BY MR. GOLDBERG: (Resuming)

Q What business are you in?

A Well I'm in the business of, I think I've stated of investing or making recommendations for the investment of, of the money of the firm and my own money in a variety of things which might include public --

Q In other words, your, in fact, in the sense of, you said a merchant banker?

A Well, that's -- yes, sir. And I've, I've also --

Q I see, and you're not a, you are not a --

A I'm not a stock broker.

Q You're not a stock broker?

A No, sir.

Q I see.

A And, and I've also been involved, as I say, in, in family, family investments and also been involved in, in a -- pricing and, and negotiating of various types of, you know, public transactions, that is underwritings, mergers, and so forth.

Q Did you know this company did have a prior dividend paying history?

A Yes, sir

Q Did you take that into consideration?

A Well as I understand it, that, that they, they -- when they recapitalized in 1968, they I think put $2,150,000 into preferred stock, of which they had under their charter a 5% dividend requirement. And that amount from the figures I got was greater, that is the 5% of the $2,150,000 or whatever it was, was greater than the amount of dividend they had paid on their prior preferred and common before this 1968 recapitalization. And that, as I understand from, from Standard and Poor's that the sheet I got that, that after the company went public, that is after the 1969 recapitalization, they did not pay any cash dividends at all on the common.

I don't know if that's accurate but that's what Standard and Poor's --

Q I don't know myself.

A That's what the Standard and Poor people say.

Q Isn't it true the only basic difference between the Class A and the Class B was the voting?

A As, as far as I know.

MR. GELFAND: Your Honor, we have stipulated the Charters of the company on the recapitalization in '68 which specifically sets forth --

THE COURT: I assume that's, that he's preparing to lead up to another question, I guess --

BY MR. GOLDBERG: (Resuming)

Q So the only difference you say in -- the only difference in the -- in the two different classes was the fact that one was voting and one was not voting, is that correct?

A As I understand it, that was the formal difference. Yes, sir.

Q All right. You used a -- in your report you say that your pro forma earnings would have been $4.71 a share for 1967 and using a multiple of that time of 10 to 12 times earnings which would -- you'd recover something like $47 to $50 a share and you've discounted it all the way down to 5. So, in other words, you have about a 90% discount for the

MR. GELFAND: Just one question.

FURTHER REDIRECT EXAMINATION

BY MR. GELFAND:

Q Do I understand that the question of liquidity versus locked-in position is the most important factor in making an investment in a closely held company?

A It is the most factor in, in not making an investment, or --

Q No, in making the investment, the question of liquidity or the question of being locked in.

A Well, I'd, I'd say that, that it's certainly the, the first thing that comes to mind, uh, you know, I think the mentality of the, of the -- of the sophisticated investor is that, you know, if, if he goes into the market and he buys shares of a company with, with a quoted market and he doesn't buy sufficient numbers so that he feels that he can't get out, then he always, you know, feels he could barring disaster, he can take his stock certificate, give it to someone, and get some cash money in his pocket. And I think that's a lot different than in a situation where you're sitting there with your, your, your stock certificate and you've got no place to go and there's no, no money coming in for holding this thing.

MR. GELFAND: I have no further questions, Your Honor.

THE COURT: Thank you Mr. Wit.

THE WITNESS: Thank you. Oh --

MR. GOLDBERG: Uh, just, just -- just one very brief question.

FURTHER RECROSS EXAMINATION

BY MR. GOLDBERG:

Q In other words, you've made your approach on the basis of a sophisticated investor, I gather?

A Oh, that's a little presumptuous, but I suppose --

Q Aren't you sort of narrowing your a, your field?

A Well, I -- No, I, I, I was understood that, that what I was asked was a willing and knowledgeable investor.

Q A willing and knowledgeable investor.

A And, and -- and that a willing and knowledgeable investor was, was one who, who had -- wasn't just the local dentist but was, was somebody who, who had seen a number of investment possibilities of different types and who had a choice about whether to put his money in a -- I assume he's in that business -- and, and, this is the one or another one, or another one and felt also that if he put money in this one that, that, you know, the next day, the next week, he'd have other opportunities.

Q So in other words this is not the, the general public in the sense that -- the buying public for stock. This would be --

A Well because the general public doesn't buy this

sort of thing. This is special business, specialized business in my view.

Q Isn't -- would you say that at this particular time in the market you probably could sell almost any, anything that is coming across the board.

A I'd say at that time, you know,if, you know -- you could even have sold a dead cat, you know, without earnings.

MR. GOLDBERG: Thank you. I have no further questions.

THE COURT: Thank you, Mr. Wit.

THE WITNESS: Thank you, sir.

THE COURT: Do you want to go ahead gentlemen, or do you want to recess now, or -- I guess you have --

MR. GELFAND: We might as well recess for lunch, Your Honor.

THE COURT: Yes. Do you think you can get back by 1:30 or --

MR. GELFAND: Yes, Your Honor.

THE COURT: Is that enough time for you, Mr. Goldberg?

MR. GOLDBERG: Oh, plenty, it'll be sufficient.

MR. GELFAND: Yeah, you go right upstairs, it's easy.

THE COURT: We'll, uh, we'll recess then until 1:30.

THE CLERK: Rise please.

A F T E R N O O N S E S S I O N

THE CLERK: Be seated gentlemen.

THE COURT: Call your next witness, Mr. Gelfand.

MR. GELFAND: Mr. Smith, please.

THE CLERK: Raise your right hand. You do solemnly swear that the testimony you are about to give in this case to be the truth, the whole truth and nothing but the truth, so help you God?

THE WITNESS: Yes, sir.

THE CLERK: Be seated. State your full name and address for the record.

THE WITNESS: Gordon Smith, 29 Neville Street, New Shrewsbury, New Jersey.

G O R D O N S M I T H, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Smith, we have stipulated your qualifications and background as set forth in your appraisal report and we shall not go into it at this time. I wonder if you could summarize briefly the procedures adopted and the basis for your valuation and how much it was for the Class B common stock of Modern Maid Food Products Inc. in August and September of 1968.

A Yes, sir. The approach I adopted in this appraisal was to value these shares on the basis of information I could gather that was publicly available concerning the prices paid of similar securities in the market.

The first step in my examination was to determine whether, in fact, there were securities of publicly traded companies, uh, being sold in a public market of companies which were comparable to Modern Maid. My search indicated that there were not, in fact, any companies which were truly comparable to Modern Maid in, in size and in nature. I did, however, look at several companies that I've cited in the food industry, more particularly manufacturers of consumer goods in the grain products area. I did this to satisfy myself that this particular industry was not being viewed by public investors as a special situation. That it was not a so-called glamour stock or in a depressed market. I did so satisfy myself and I concluded after some examination of, of Modern Maid's financial and operating data for, uh, for the years that I had available to me that I've, uh, cited in my report. I concluded that an appropriate price to earnings ratio for Modern Maid stock if it were on a public basis would be 10. This was based on my practical experience with some consideration of the general conditions of the market at the time. I applied this price earnings ratio of 10 to the average earnings -- net earnings

of Modern Maid for the years '65 through '67. I felt that this is the information that would be available to a prospective investor in these securities. The value I derived by that was $6,160,000 which represented to me the fair market value of the equity of Modern Maid if it were being actively traded in a public market.

These securities are not in fact, or were not in fact, being publicly traded. It was a closely held company and I felt an adjustment was warranted to that extent. One measure of this adjustment which has been used is, is the costs incurred in the, the process of going public and offering securities to the public market, including underwriting, commissions, fees, legal fees, accounting fees, and the expenses of the management of the company during the, during the public offering period. I concluded that a discount considering those factors of 15% would be an appropriate adjustment for the non-liquidity inherent in the purchase of a closely held security. Applying this discount to the value that I previously derived, I arrived at an adjusted value of $5,236,000, which represents the fair market value of this equity with consideration of its closely held status.

Now this equity included some preferred stock at that time. I looked at some other issues of preferred stock in companies that, while they were not in a similar business

to Modern Maid, were -- had a rating, like this, this Standard and Poor's rating as a matter of fact, similar to what I thought that Modern Maid would carry if it were rated. The rating of triple B or double B. I found that these investors in these securities were requiring a 6.4 average return on their investment. Modern Maid carried a $5 or 5% return on its investment. Carrying this through in a calculation, I concluded a value of $80 per share, which is what an investor would pay in order to ins-- assure himself of a, of a 6.4% return, as indicated by the market. This would indicate that the value of the preferred shares of Modern Maid was $2,016,000. I subtracted that from the $5 million-odd dollars and arrived at a value for the common shares of $3,220,000. I utilized the number of common shares as 108,000 in my calculation and dividing that out, you get $29.81 per share on that basis. This to me is the value of the common shares of Modern Maid if an investor could purchase a minority interest in the closely held stock of Modern Maid of one single class of common stock with a typical rights of receiving dividends, voting rights and, uh, capital distribution.

This, however, is not a possibility with Modern Maid. This was a single class of common stock that we're appraising here that did not have these typical rights. So, again, I felt that an additional consideration should be made for

that fact. I looked then at the records of some of, of some other investment companies, or funds if you will, that were formed actually during 1968 who specialized in investments in restricted closely held securities. And I examined them, where I could for the value line, Development Capital Corporation, which had been in existence long enough to have purchased some of these securities and have some experience. And I compared the price that they paid for shares of restricted unseasoned small venture companies with, in particular cases, of the shares that those companies had issued which were free. In other words the fund was buying restricted shares where the company already had some publicly traded issues. And I compared on the date the price they paid for the, uh, restricted shares with those that the free shares were selling and I found that, uh, discounts ranged from 16 to 70 percent, with the average being 44. If I look at the, the upper-half of these, I found that half of the securities were over 40% discount and they had an average of 57. Now I considered also in examining these that the prospectuses of these funds and I noticed that in several cases the funds in purchasing restricted securities of unseasoned companies had sought to reduce their risk by, uh, at the time of purchase negotiating an agreement with the issuing company that at some future date they could force a registration and there would be a public market for their shares.

I found that some of the funds reduced the amount of this type of security which they would purchase. Both of which are ways that they sought to reduce the risk of really liquidity, as we heard Mr. Wit mention this morning. They sought to, to assure their liquidity in the future.

After consideration of these facts I concluded that a, an appropriate discount to be applied to the Class B common shares of Modern Maid would be 60%. I applied that discount to my per share price of $29.81 and the computed result is $11.92. I concluded, therefore, that the fair market value of the Modern Maid shares being appraised as of August and September 1968 as $12 per share.

MR. GELFAND: May I have this marked for identification, please. May we use the original, Your Honor.

THE COURT: Yes.

** THE CLERK: Petitioner's Exhibit 18 marked for identification.

BY MR. GELFAND: (Resuming)

Q Mr. Smith, is this the report you have prepared in connection with your appraisal of the Class B common stock of Modern Maid Food Products Inc.?

A Yes, it is.

MR. GELFAND: Your Honor, I submit this in evidence as Petitioner's Exhibit 18.

** THE COURT: It will be received.

(Whereupon, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 18 was received in evidence, as described above.)

BY MR. GELFAND: (Resuming)

Q Mr. Smith, you arrived at a figure of approximately $12 a share when you divided through by 108,000 shares, um, making allowance for the additional 4,790 shares that had been sold, so there was a total number of shares outstanding of 112,790, do you know what your appraisal value would have been?

A It would be approximately $11.50.

Q Referring to your report on page 9, on page 9, you state that a certain group of companies were most closely representitve of Modern Maid Food Product Inc. Would you please explain what you mean by most closely representative.

A Well, I feel that, uh, these companies are first part of the, the food industry, as I noted, and, and more specifically they are involved in the processing of grain products and to that extent I feel that they are representative of, of Modern Maid's business.

Q You mean those were the closest you could find

representative, you don't mean that they are, well -- Do you mean that they are most closely representative or that they are the most closely you could find?

A They're the most, most closely I could find. They're the best of a poor compromise, I think.

Q Referring to the last paragraph on page 12 and the top of page 13, does your valuation presuppose Modern Maid Food Products going public?

A Yes, it does.

Q All right.

A I have assumed that a prospective purchaser of these shares would be betting, to use a word, that the company would, based on its size, its business, the, the general characteristics of it that anyone could know in a public way.

Q Suppose there was no intention of going public, would that fact have -- factor have of had an effect on your valuation?

A Yes, it would.

Q What effect would it have had?

A Well, as I say, I've assumed that an investor would assume -- would go on the basis that it would within 2, 3, or 4 years. Uh, if there were some assurance to the contrary, it would certainly have an effect, it would reduce it substantially.

Q Would you be able to say how much substantially, or how substantially?

A Well, in my opinion, uh, an assurance of that kind would place this stock in the class of a, of a highly speculative, uh, security and, uh, I guess I would have to defer to those who are in the marketing area to know what a, a highly speculative issue might sell for.

Q I direct your attention to page 18 of your report, the second sentence in the second starting paragraph that starts on that page. Value Line has stated that it is a policy that at least 50% of the value of restricted securities in its portfolio must be the subject of a commitment from the issuer to registerer at Value Line's request, the securities, under the Securities Act of 1933. Do you know whether any such commitments existed with respect to the securities listed in Table 3?

A No, I do not.

Q Did you in your appraisal assume that they did exist, that some of them did exist?

A Yes, I did. I assumed that there were some in there that did have such an agreement, but I don't know the exact number.

Q Referring to Exhibit 3 in your report, do the restricted securities listed there have a public market for their shares, I mean for the free shares?

A Yes, of the --

Q In other words, these are restricted val -- discounts that are obtained on stocks that were already being traded?

A Yes, I selected these from that portfolio for that purpose.

MR. GELFAND: I have no further questions, Your Honor.

THE COURT: Let me ask the witness -- Mr. White in, in making these a -- in allocating your residual value between the Class A and Class B, did you give any consideration at all to the fact that less than one year later when it became necessary to make a similar allocation in connection with the public offering that the ratio was 7 to 6.5?

THE WITNESS: I was aware of that allocation, uh, frankly I did not consider it, I did not know what the source of that was and why that decision was made at that time.

THE COURT: In other words, you made no effort to try and account for the disparity between what was presumably an arms length division of the residual equity at that time with, with your determination?

THE WITNESS: That's true.

THE COURT: Mr. Goldberg.

CROSS EXAMINATION BY

MR. GOLDBERG:

THE CLERK: Please be seated. State your full name and address for the record please.

THE WITNESS: Herbert S. Cannon, 140 Tekening Drive, Tenafly, New Jersey.

THE CLERK: Would you spell your last name for the record?

THE WITNESS: (spelling) C-A-N-N-O-N.

H E R B E R T S. C A N N O N, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Cannon, the parties have stipulated to your qualifications and experience and we'll put the same question -- briefly could you summarize the procedures you used in determining what the Class B common stock of Modern Maid Food Products Inc. would have sold for in August and September of 1968, under the facts -- existing at that time.

A Well I took a general overview first of the company, examined its operation and its history to date. I evaluated the investment climate at that time, uh, what asset values were, and what discounts might be applied; the, uh, type of security; its lack of marketability; it's, uh, lack of exercising control even though it was a substantial portion of the overall equities outstanding; its lack of dividend; the

limited growth of the company at that time over the past 3 years or 4 years; uh,what possibilities might exist principally for a purchaser or a group of purchasers to derive a profit from buying this stock and why would they get involved in the first place. In other words, could they force or seek or look to management to go public to sell out to somebody else, to merge with a public vehicle, to liquidate the business and retire, and what values might come up, uh, if they took any or all of those approaches. The general age of the principles, the sibling factor in the company, uh, also the amount of money that might be required to take a position in the company, uh, the cost of that money to the investor, and the time parameters pursuant to which he might be able to either retrieve the money and a profit and what would induce him to look towards getting that profit.

I looked also at underwriting conditions at that time. Uh, the, as I said again, the price earnings ratio or the value of the stock. I took a discount of the value of the preferred stock and its return to come up with a gross value for the common -- for the non-voting common. I then considered the liquidity factors under the existing securities regulations at that time and, namely, Rule 154, and the ability even if it did go public and even if its class was changed, none of which were factors at the time, uh, how long it would take to liquidate under the so-called

1% rule at that time where you could only sell a limited amount of shares every six months and then not on a regular basis. The fact that it had no rights of registration and that the company could never force any had it gone public. Uh, I considered the prices that I have been involved with in private companies and public companies for paying for stocks, not necessarily similar industries although I had some involvement with this industry and with, uh, a company similar to it, and how much discount which -- and what profit potential you would have to minimally look for. Uh, the number that I used is that you must make within a 3 year period of time, 4 times on your money, or at least hope to make or you shouldn't get involved with an investment to begin with. And in doing that, you have to anticipate an actual ability to liquidate at whatever price. In this case there was no factual, at that time, ability to liquidate. Where I talk about a 4 times profit on your money within 3 years is where there might be defi -- there would be definite rights of registration, or a definite sell out, or a definite contractural obligation by the company to pur -- repurchase this stock in the event they don't do any of the other things.

Uh, in putting all those together, I would come out with a very nominal value that I might, as a speculative investor pay for it with the hopes of pushing management

towards doing something, and a value of about $2 a share, which is a very substantial discount from book. If I could assume that management would be very cooperative and that I would be able to liquidate within the 3 year period of time, I came out with a value between $5 and $6.50 a share. Uh, in my opinion, any price above that would be a, an extremely whimsical and speculative investor -- investment for an investor to make. And I personally wouldn't advise a client to do it.

Q Mr. Cannon, referring to your report, I wonder if you could clarify a little more what is -- you intend on the bottom of page 6 and the top of page 7 when you state, what must be emphasized here is the purchaser of a Class B common stock, non-voting, without the ability to force management to change the status of the stock from non-voting common to voting common could entertain no probability of ever liquidating the stock in the public market. Due to different class status none of the rules of the S.E.C. or ~~any~~ N.A., S.D. -- is that the National Association of Security Dealers?

A Correct.

Q Permit an automatic registration, even after a substantial holding period, to enable even piecemeal liquidation to the public -- into the public market. I wonder if you could clarify what these rules are, why if you have

a company that is already public that these shares couldn't have been sold, even on a piecemeal basis. I wonder if you could explain that.

A Well, that takes into consideration two situations. If you own non-voting or a separate class of stock and that stock has not been registered for public sale, you can't put it out until it is registered into the public market without the company cooperating and going through a registration for you. So you have a total lack of liquidity in the open market and you could only dispose of it under an investment letter and a private sale. If the company -- if you had a class of stock that was equal to the other classes of stock that were public, then you could only liquidate in the public market if there was a registration, whether it be what we call "shelf" meaning you've got six to nine months to liquidate it in the open market, or whether done through an underwriter at a fixed price, or agree to a price, or during 1968 you could liquidate under 154 no more than 1% of the total capitalization outstanding during any six month given period of time with the further -- further carry out being in the law that you could not do that on a regular basis that every six months you sell 1%. In this case there was -- after the recapitalization there's a million shares outstanding, they could sell 10,000 shares every six months, but if you did it for more than a year

and a half or two years, and you sold more than 30 or 40,000 shares that way, the S.E.C. very likely would come in and tell you, hold up for a couple of years and don't do it again, because it can't be part of a regular pattern. That law has since been changed recently into what the new 144 regulation that does permit a 1% liquidation on a regular basis every six months. And you can go on infinitum until you liquidate your total position.

Q A hundred years.

A If you own that much stock.

Q Oh, it's 1% of the total capitalization of the company, is that --

A Right. And that's further restricted by the -- in some ways by trading volume, if it's listed on a national exchange. So it could be even less than 1% in some circumstances.

Q This procedure of, you say an investor seeking 400% profit or $5 back for each dollar invested -- in your experience do these situations actuall prevail during the year '68? In other words, I understand from your --

A It's very common.

Q History, you were active in that and I was just wondering whether you knew of any?

A Yes, I was active as a stock broker and running a brokerage firm and more specifically running its corporate

finance department. And we, uh, had put together and did several private placements with that anticipation and in many cases with that realization.

Q Your value of $2 is based -- I'm reading this -- is based upon the fact that it would require -- because of the number of shares it would have required a tremendous amount of dollars to put in which would restrict the number of buyers?

A No, that's only one phase of it. The, the fact you would have invested close to $200,000 or $180,000 or $190,000 without any return, but more important without any chance other than making a total nuisance of yourself some how to force management to take you out, or somebody to take you out, or hoping to find, uh, in the hey days of '68 where everybody had a lot of loose money, of finding another investor who you could sell it to under an investment letter. Now these possibilities have kind of limited it. I, I've seen cases where somebody has owned over 51% of the stock of a company and couldn't force themselves on the board, after spending hundreds of thousands in legal fees. So, you'd have to just say that you're going to go in and either be friendly with management somehow and, uh, or have a heck of a lot of extra cash and say I'll wait out 5 years, 2 years, 10 years, whatever it takes until they liq -- eventually liquidate this business and try and make a profit. In that

case you've got to make more than 4 times on your money because your possibilities are extremely limited. And as a practical person, I wouldn't put a couple hundred thousand dollars in something that I couldn't have at least a, a definite probability of coming out whole within a 3 year period of time.

Q In other words you're -- But you feel that there would be always somebody who would put something in --

A There's always somebody and, and at $2 it's probably a good rank speculation and I might've recommended it to somebody if, if they were akin in the industry and thought that they could, you know, back door themselves together or had some in -- some other interests in it.

Q Now, assuming, you mentioned something about coming out whole or liquid in two or three years time, uh, then the value would be, is that $5 or $6, is that what you're saying?

A Yes, sir.

MR. GELFAND: I have no further questions. Oh, wait, I'm sorry, Your Honor. I forget sometimes. I did it twice today.

BY MR. GELFAND: (Resuming)

Q Is this -- Mr. Cannon, is that a copy of your report that you based your appraisal on?

A Yes, sir, it is.

In other words --

THE WITNESS: Substantially the same, yes.

THE COURT: 49% of voting stock in a, a --

THE WITNESS: It's almost as useless --

THE COURT: In a corporation where the other 51% is owned by someone else is, is subject to the same inhibitions as this. Is that --

THE WITNESS. Basically, yes, sir.

THE COURT: All right. Now isn't it true though in a, in a -- this was a New York corporation that -- that under those, those circumstances the, the owners of the majority control of the voting stock owe certain obligations to the minority interest?

THE WITNESS: Well to the extent that any, uh, Director or officer or majority holder owes it to his minority shareholders. In other words they can't go out and declare themselves million dollar salaries, just so nothing would be left, they couldn't just give away the net assets of the company, or any minority shareholder could come in and take action to stop them. That's what I meant when I referred to creating a nuisance of themselves to try and force them to, uh, liquidate a position for a profit.

THE COURT: Well aren't there people who have done this with considerable success?

THE WITNESS: Absolutely. Some people thrive on it.

The Court: So one of those might pay a considerable amount more than $2 for this stock, wouldn't he?

THE WITNESS: I sincerely doubt it. Uh, they would want to, in that case, make at least a 10 to 20 times profit based on marketability because they have to couple that with the fact that they are either usually attorneys and can do it themselves or have to hire attorneys at considerable expense to get the job done. And, and that's all time consuming and expensive and they generally will have a little more patience and very often can wait 5 to 7 years before they see a return. So, I doubt that they'd pay much more than 2, if that. Two is certainly what I think.

THE COURT: Mr. Goldberg.

BY MR. GOLDBER: (Resuming)

Q Mr. Cannon, how was the stock market in 1968?

A Sensational.

Q Sensational. How were new issues coming out?

A Cheaper by the dozen. They were coming out, uh, quite furiously and at very high PE ratios.

Q In other words, 40, 50,60 times earnings is --

A Well, no, the ones you read about that way -- most of the companies that have no earnings and no history of earnings, if you're going to compare it to a company that's been in existence for a while --

Q Right.

wouldn't sell to me for $2 a share.

Q So in other words, your $2 a share is strictly on what you personnaly would buy it for.

A It's what I think a buyer in, uh, in that class would pay for it. That's correct.

Q I see. Uh, so in other words, you've given the stock, the Class, uh, B non-voting stock approximately about a 95% discount?

A Off of book?

Q Off of -- no, off of your value of $33.70, if it was public?

A Under that set of circumstances, yes.

Q Or, but just for the fact that it was non-voting?

A No.

Q Not, not --

A Not just for the fact it was non-voting.

Q It was non-voting and, and it, it -- you say if it was public, it would be worth $33.70 a share, right? If it was marketable?

A No. If it was fully marketable, at that time, uh, yes. I guess that's what I came up with.

Q Right. In other words your discount is based on the fact that it wasn't marketable and it was a Class B stock? Non-voting.

A And had no ability to become marketable and a

Class A stock.

Q Well, yeah, but see you make a statement here, for public offering or merger with a public entity could not be reasonably expected within a three year period, and I would be loathe to invest more than $2. Now suppose it was reasonably expected it would go public?

A I would pay more than $2.

Q How much would you pay?

A As I came up to my price, at between $5 and $6.50 a share.

Q Did you know the following year this same class of stock, after it had been capitalized, was sold for $78 a share?

A That's correct.

Q And you still would only pay $6 six for it?

A I wouldn't have paid what the underwriter paid for it at the time it went public, personally.

Q You were associated --

A As an underwriter.

Q What -- you were asssociated with, uh, at one time with Weis, uh, Voisin, Cannon?

A Weis, Voisin & Cannon. I was president. Yes.

Q What happened with that company? Is it still in existence?

A No. I retired in '69 and it, uh, folded in 1972,

the end of '72.

Q So, based on your experience, uh, someone would expect at least a 400% return within a three year period at this time?

A Yes, sir, on private placements.

Q Uh, Did you ever recom -- recommend any investments that returned that high?

A Yes, sir.

Q A number of them?

A Several.

Q By several, how many do you mean?

A I can list them. Uh, I would put it to you this way, any one that we ever did in the form of a private placement, we expected at least that return, or we would not have done it.

Q Well, were you ever satisfied, that you did get 400%

A Oh, yes. I've got, uh, 1400% and, uh, more on occasion.

Q On occasion, but I mean for a company like this, what would you expect to return? Would a --

A For a company like this, as I said, I would expect at least a 400% return.

Q Wasn't that sort of unrealistic?

A Not at all. I think if you tie up money and you're

locked up and you can't quickly get out, and that's with an anticipation that you have an ability to get out; in other words, when we do a private placement we have a right of registration at the company's expense. So that the company between the 24th and 36th month must register stock for us, or we'll have an, a built-in ability to sell it back to them. And based on its road, or rate of growth, during that interim period of time and what it's done with the money we've put into the company, uh, we project out our return. It doesn't always happen. Uh, on 11, I believe, private placements I did while President of Weis, we broke even twice; we, uh, made 200% on the money within two years on three occasions; and we made better than 400% on the rest.

Q Uh, do you know that the 196 -- are you aware that in 1969 in June, there was a recapitalization?

A Yes, sir.

Q And all these shares became one class?

A Yes, sir.

Q And there would be no distinction in voting?

A Yes, sir.

Q And they'd all be the same class of shares?

A That's correct.

Q Uh, would that have had the effect on your --

A Absolutely. Uh, if it was all one class of stock

identification.

MR. GELFAND: Your Honor, may I call Mr. Silverman back for two questions?

THE COURT: Certainly. Certainly.

MR. GELFAND: To, to clarify something. Jack, will you take the stand.

MR. SILVERMAN: Thank you.

MR. GELFAND: He's unaware. I haven't spoken to him. It may be bad policy.

THE COURT: You've been sworn now Mr. Silverman just take a seat there.

MR. SILVERMAN: Thank you.

FURTHER REDIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Silverman, since December 31st, 1967, has Modern Maid Food Products Inc. paid any dividends on its common stock?

A To the best of my knowledge and belief, I don't believe so.

THE COURT: Maybe we'll aver another case.

BY MR. GELFAND: (Resuming)

Q Maybe the time is a question, we have stipulated that none -- no common stock dividends were paid in 1968. Were there any common stock dividends paid after 1968?

A No.

Q Okay. Thought the year might throw him. The -- I don't know if you've had time to think it over, but did the stock that was subject to gift, was there any repurchase, buy out, or buy back agreement with respect to the stock that was given to the trusts?

A No.

MR. GELFAND: That's all, Your Honor.

THE COURT: Thank you, Mr. Silverman. The Court had marked as Respondent's Exhibit O, a valuation report prepared for the respondent by the Manufacturers' Appraisal Company and it's noted that -- there the report concludes that the value of the stock as of the basic date was at $25 a share. Is that right?

MR. GOLDBERG: Your Honor, did I hear you say the Court concludes?

THE COURT: I, excuse me, I mean the report. The report I said, the report concludes that it was $25. Is that right, Mr. Goldberg?

MR. GOLDBERG: That's right, Your Honor.

THE COURT: So, uh, we -- and I, I don't recall any valuation case where the Court found a lower value than the petitioner's highest witness, but I'll, I'll look for that. So, aren't we -- aren't we somewhere within a range now of between $12 and $25, Mr. Gelfand?

MR. GELFAND: No, sir. In a --

Carter I think it was.

Q That's the United States District Court of the Southern District of New York?

A Yes, that's correct.

Q Mr. MacMullan, would you briefly describe -- well, Mr. MacMullan, what is the value of the stock of Modern Maid Food Products on the critical gift date, that you arrived at?

A It is my opinion that the value of the stock is best expressed as $25.00 a share.

Q And, how did you arrive at your valuation?

A I think it would be best if I very briefly ran through the appraisal report itself, I won't dwell in great detail on the pages since it is there in writing to be read, but if we would turn first to page 27, which is actually the first page that begins the valuation, I have taken three approaches to valua, one of which I feel is more pertinent than others. But, the first approach here is a return on net worth approach, which simply compares the return that the subject company was making on its net worth, to the return that several -- five in fact, comparable companies were making in their net worth, an excess return is apparent, and that is capitalized at an intangible rate of return to determine the total value of the company.

The total value of the company based on that

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approach, the value is $5,200,000.00.

MR. GELFAND: Your Honor, may I please have a voir dire on the witness's qualifications, there are a few points I think that should be clarified?

THE COURT: All right.

VOIR DIRE EXAMINATION BY

MR. GELFAND:

Q Mr. MacMullan, in looking at Exhibit O, it is apparent that most of your activity, almost all of it, has been in the field of appraisal in real estate. You do mention that you have appraised stock in closely held corporations, can you please describe the nature, the activity of those stocks, were they real estate corporations?

A No, they are not real estate corporations. I think that the qualification sheet that you see there is somewhat misleading in that the large quantity of the items on there relate to real estate, however, for the past six years my primary employment for the Manufacturers Appraisal Company has been the valuation of intangible assets, including the stock in closely held corporations.

Q Well, what I am trying to find out is what is the activity of the closely held corporations, were the closely held corporations principally real estate corporations?

A No, they are principally not real estate corporations, and they have run the full gamut of --

Q Could you give me a few of the names, just a few of them, please?

A I could give you a detailed list of 15 or 20 of them, if you would like, I don't have them with me.

Q Well, would you know the names of three of them, and what fields they were in?

A I'm not sure, let me think. Well, let's see, Smith Lumber and Supply Company, they retailed lumber supplies. And, quite frankly I'm stuck for the names of -- of these companies, I would be happy to give you a full list of every company that I have appraised in the last 2 years, and you will find that, you know, they run the complete gamut of different types of industries, and so forth.

Q Have you had any actual experience in counselling purchases of securities of closely held companies?

A Not in the purchase of them, I would say yes in the sale of them. One of the reasons that people want appraisals for the stock in closely held corporations is to decide what they should sell it for. They may be considering going public, they may be preparing a trust of some kind, or they may be preparing -- you know, for a personal estate. And, they come to us frequently and ask

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mony of my witness.

THE COURT: You may, you may.

DIRECT EXAMINATION BY

MR. GOLDBERG: (Resuming)

Q Mr. MacMullan, have you -- do you remember where you left off?

A Yes.

Q Okay, would you please pick up again?

A I would like to go to the second approach that I took, which is a price earnings ratio approach, and it is on page 29 it starts.

It simply compares the price earnings ratio of five comparable publically held companies to the -- and applies that ratio to the earnings of the subject company for the year ending December 31st, 1967. That produces a total value which is then discounted for lack of marketability that discount being determined by the actual cost of location of a common stock issue of that size.

Skipping over to the next approach, is a comparable public enterprise approach we call, it, it begins on page 32, and that is really quite similar to the price-earnings ratio approach, except that it considers two other factors as providing some evidence of value, and that includes net worth and sales, in addition to earnings, and develops multipliers and applies them to the subject company's earnings,

net worth and sales, and once again, discounts the total value of the company so determined by an 8 percent amount estimated to make the stock public.

So, at that point we have run through three approaches and it was my opinion that the last one, the comparable public enterprise approach provided the best insight into the value, and that the $7,000,000.00 figure was the best estimate of the total value of the subject company.

We then reduced this in value, in an attempt to determine the value of the class B common stock, we subtracted off first the value of the preferred stock, the cummulative 5 percent non-voting preferred stock, and I used the $100.00 redemption value, even though I realized that the amount of interest that that stock would -- the 5 percent interest was somewhat below market, and that stock would probably actually have sold on the open market for something like, oh, $75.00 or $80.00 a share.

But, I used the full amount because in fact it was redeemed a year later, and perhaps there was some indication that that might have taken -- was going to take place. Anyway I subtracted off the value of the preferred stock, that's $2,520,000.00, and leaving a residual value to all the common stock, both class A and class B, of $4,480,000.00. Strictly mathematical division of this total

value by the total numbers of class A and class B shares produces a total value per share of $40.00.

However, we realize that the class B is both a minority interest, or rather the subject stock is both a minority interest and it is class B non-voting, so there is some further discounts to be taken into consideration.

I've used 25 percent as the best indication of the proper discount for the minority interest, and there is a study of two step acquisitions contained in the addendum of this report, which is my basis for utilization of the 25 percent. An additional reduction in value from -- at this point we are at $30.00 a share, and I've taken off another $5.00 a share for the fact that it is non-voting. I'm not really sure whether this is correct, since the elements that are missing for both non-voting -- for both the class B and the minority interests are the same thing, that's a lack of control, but at any rate, I guess there really is something to be said for the fact that the class B minority interest is worth less than a class A minority interest, because the potential for control doesn't exist with the class B, you can't form any kind of a combination with anyone else, and get control of the company, so I've taken a $5.00 per share discount, or a reduction in value from that, and that is how I got the $25.00 a share.

I think that -- that there is two points that I

would like to go into in some detail, and I know that you probably will want to talk to me about it on cross examination anyway. And, I really feel that the comparables that I used I must talk about those and explain why I used them, and I do want to go into a little bit more detail about the discounts taken.

I readily admit that the comparables are really not comparable to the subject company. We found in fact no companies that were really comparable. And, nevertheless though, I feel that -- that the five companies that we did select are useful, and that they can be helpful in estimating value. And, maybe if I go over some of my reasoning it will become clearer.

I had available to me the Prospectus, which is dated October 28th, 1969, and on both page 3 and page 6, it outlines what the subject company did, and it explains that they manufactured breading and batter mixes prepared to customer specifications for food processers, and that they also manufactured fully prepared flour mixes that required the addition of water before baking for use in restaurants, hotels, hospitals, and other institutional mass feeding outlets.

And, it also outlines that breading and batter mixes for 1967 constituted 55 percent of the sales of the subject company, and that prepared flour mixes constituted

approximately 43 percent of the sales for that year, 1967.

And, also on page 7 it mentions that the principal raw material that the subject company used was wheat flour.

Now, we already -- the study that we made, we found that there was really no companies that made, at least no comparable publically held companies that made breading and batter mixes, that were in the size range of the comparable, of the subject company. And, so we know right away that 55 percent of the company's business is really not comparable to that of a listed company.

So, we are down to looking for companies that make prepared flour mixes, or perhaps that have wheat flour as a principal raw material, or who might be selling to similar customers. We are looking for sort of second echelon comparables here, for something that is comparable, secondary,or an indirect way, but which might still be of some use, or some help to us in determining value.

Another factor that I felt was important was to find comparables that are roughly in the same size. I realize that Phillsbury,General Mills and DCA Industries are competitors of the subject company, or were competitors of the subject company, but I felt that they were so large that -- that -- and they were into so many diverse fields, that to make comparisons with those companies is really not

meaningful.

Now, in the addendum of my report between pages 37 and 43 --

MR. GELFAND: Your Honor, I think that it is apparent from the witness's testimony and from examination of pages 37, 38, 39, 40, 41, 42, and 43, dealing with his comparatives, that they are, with the exception of Martha White which may overlap a little bit and I think that the witness will bear out that what they sold was in the retail field, there isn't any one that even approaches what the taxpayer does, and it isn't a question of using it as a guide, but what he did was actually take their figures and statistically apply it to our taxpayer, and I therefore say that this whole report is based on facts that are completely foreign and irrelevant to our situation, and I move that the report be striken.

THE COURT: Your motion will be overruled. I think, Mr. Gelfand, that this all goes to the weight to be given to the witness's testimony.

MR. GELFAND: But, they are -- all right, we'll do it on cross, Your Honor.

THE COURT: Because -- I think actually this isn't the first time that we have had to determine the fair market value of a company with respect to which there are no comparables, public listed securities to use as a guide. Now,

that's done all the time, and the witnesses can make all kinds of approach to that, and when you get down to deciding as to whether or not you are going to accept their conclusions, why you look and see whether their approach makes any sense, that's all, isn't that right?

MR .GELFAND: Your Honor, I can understand as a guide to get some general feel, but this witness has done more than that, he has taken their figures, and interpolated them against the actual --

THE COURT: Well, that the Court will take into consideration. And, I would assume for example that Mr. Silverman could probably successfully do what Martha White does, if he put his mind to it. And, I would suspect that they probably put the same thing basically that he sells in a cardboard box and it goes on the grocery shelf, now the formulation may be different, but they have obviously an acceptance or a trade name, or a tie in with Safeway, or something that enables them to sell that way.

BY MR .GOLDBERG: (Resuming)

Q If you would continue, Mr. MacMullan?

A Certainly. I was going to mention that between pages 37 and 43 of the report, are outlines of the comparable public enterprises that we used, and there is a brief summary of the business -- the type of business that those companies do.

I feel -- I admit that they are not comparables, however, frequently this is a problem that we have when we are faced with making a valuation of -- of stock in a closely held corporation. Frequently there are no comparable publically held companies, so we do the best that we can.

I don't think that the -- that the -- the earings multiple for example of 14 that I utilized is necessarily high or necessarily incorrect, and I offer this next statement only in a confirmatory way, it -- it didn't contribute to my utilization of the 14 multiplier, but I note that in 1969, the $12.00 a share public price, is about 14.4 times the 1968 earnings. So, it is not necessarily wrong. And, I didn't - - I didn't use that 14.4, in fact I really didn't become aware of it until I had developed by own figures, but I do offer it in the way of confirmation of the reasonability of the answers that we did get from utilizing these comparables.

The next subject that I would like to just briefly touch on is the discounts that we used. We used three basic discounts, one for lack of marketability, of 8 percent, one for the fact that the stock was a minority interest of 25 percent, and one for the fact that the stock was class B non-voting stock of $5.00, which if expressed as a percentage would be about 16 2/3rds percent.

I think that the total discount taken is -- is

reasonable, and -- and I enclose in the addendum of the report starting on page 44 some Court cases that touch on the discounts for fair market value from stocks, in closely held corporations, and I don't think that any of these total over 50 percent, and if you read through the cases you will see that some of those that are up about 50 percent had much less to offer than the subject company in the way of future possibilities.

I think that that ends my basic testimony.

Q Mr. MacMullan, so you have stated, am I correct, that you used these "comparable companies", as a mere guideline for in your best judgment the -- the only companies that you possibly could compare them with in size and sales and product line?

A Yes, I feel that in an instance like this you are faced with two alternatives, one taking an arbitrary price earnings multiple of some kind, and ten seems to be the standard one when somebody wants to get arbitrary, they generally take ten, or attempting to make some comparisons with companies that have some things in common with the subject, and that's the route that I chose.

MR. GOLDBERG: No further questions.

THE COURT: Well, let me ask the witness, isn't it true though, and looking also at the report of the gentlemen from the American Appriasal Company, and I doubt

remark on their most closely related, and then they were because they couldn't find anything else, he didn't take those figures and apply them, he said based on this, these are what these established companies with good will, name, good will in the marketplace, good will on their product, their diversification, their economic clout, if they sell at this multiple, what should this small little, unknown company sell for. And, then he said maximum ten times.

But, in this particular case as we review this, the witness hasn't done that.

CROSS EXAMINATION BY

MR. GELFAND:

Q Mr. MacMullan, would you say that investors divide roughly into two categories conservative and speculative?

A No, I wouldn't say that.

Q Well, into what categories would you divide the investors?

A I would say that they are probably the two extremes, and people fall into all kinds of classifications in between.

Q I know, but I said roughly those two categories, and then there of course are those in between?

A You asked me if I would say that, and no I wouldn't say that.

Q All right, what categories would you say they fall into?

A I wouldn't try to number a certain number of categories that investors fall into.

Q No, I'm not trying to get a number --

MR. GOLDBERG: Your Honor.

BY MR. GELFAND: (Resuming)

Q But what raw groupings do they fall into?

MR. GOLDBERG: I think that this is meaningless, because you can have a buyer for any kind of business, it all depends on the price, the business, the questions --

THE COURT: Well, I -- let Mr. Gelfand pursue this a minute.

BY MR. GELFAND: (Resuming)

Q Would you disagree with this statement, Mr. MacMullan, a fairly conservative investor who purchased for an investment is concerned with his powers of control, the liquidity of his investment, the opportunity to revamp the asset holdings of the company, his net return by the way of dividends, as compared with other opportunities in the open market?

A Are you asking me if I would disagree with that?

Q Would you agree with that or disagree with it?

A I would not disagree with that.

Q Then what do you believe are the criteria that

a speculative investor uses?

A I would say that a speculative investor, while he may consider those factors that you mentioned is more concerned with the immediate return or short term capital gain of some kind, something like that.

Q In other words he will just weigh the risk out of how much he will get out of it within a relatively short period of time?

A Would you say that again, please?

Q He'll weigh the risk of loss against what his possible gain would be, and the cost of carrying it if he should happen to be locked in, even a speculative investor would consider what's going to happen if I'm locked in wouldn't he?

A Yes, but you haven't said anything that's different from a conservative investor, and --

Q Except he is willing to take more of a risk.

MR. GOLDBERG: Your Honor, Mr. Gelfand is sort of arguing back and forth with the witness.

MR. GELFAND: No, I am trying to find out what criteria a speculative investor uses, or any investor.

MR. GOLDBERG: I think that we are getting far afield --

MR. GELFAND: Well, if --

MR. GOLDBERG: In the questioning, Your Honor.

THE COURT: I think that the Respondent's objection is well taken in that you have all types of investors.

BY MR. GELFAND: (Resuming)

Q Would you say any investor is concerned about the length of time that he might have to make his investment in a situation?

A Yes.

Q Is degree of risk of loss against -- weighed against the possible gain?

A Are we -- which investor are we talking about?

Q Any investor is concerned with his possible risk in going into a situation, and his possible gain that he may get from a situation?

A Certainly.

Q The possibility of liquidation?

A I would say that that is a factor.

Q The available market in which to dispose of the stocks subsequently?

A Yes, I already answered in the affirmative to this with your other --

Q All right, what criteria does an appraiser use a general rule in selecting comparable companies?

A He attempts to find companies that are comparable in as many areas as possible.

Q Size would be one?

A Size would certainly be one.

Q Product?

A Product, right.

Q The market whether it is retail, wholesale or manufacturer?

A Customers.

Q The customers that you are selling to, trade name, length of time that the company has been on the market?

A No, this would be an ideal comparable.

Q I mean these are the factors --

A Which practically never exist, but yes, you certainly love to find five that were that way.

Q All right, let us turn to your comparables please.

MR. GELFAND: Pardon me, Your Honor, I can't read --

(Pause.)

BY MR. GELFAND: (Resuming)

Q Now, let's turn to page 43, Spaulding Bakeries, Inc.

A 43?

Q Page 43. Now, what does this company do?

A You are asking me what it does?

Q Yes.

A It operates a bakery, selling bread, rolls and crullers in New York, Connecticut and Pennsylvania, under the name County Squire.

Q It it one bakery?

A I don't know, I would assume that it does not have one bakery, since it is listed as being in three States, it must have more than one bakery.

Q All right. And, what does it sell, to stores, does it have its own stores, do you know, does it sell to other stores?

A I don't know.

MR. GOLDBERG: Your Honor, this is -- Mr. Galfand is going over the comparables, the witness has testified that these are not comparable to the subject company. The Court realizes that these are not comparable to the subject company exactly, and it is his best estimate, his best judgment to use certain criteria in comparing similar companies in the sense of size and maybe the product lines, in the bakery business the same way that --

THE COURT: Well, let me ---let me ask the witness, where did you get your information as to these five companies, off of those yellow what are they Dunn and Bradstreet sheets?

THE WITNESS: No, these are from Moody's Industrial

Manuals.

THE COURT: Moody's sheets, right.

THE WITNESS: From the actual bound manuals.

THE COURT: Yes, they are from the bound manuals, so that the only information that you know about these companies is the information that you got from Moody's, is that right?

THE WITNESS: That's correct.

THE COURT: Okay. That short cuts that.

BY MR. GELFAND: (Resuming)

Q Would you say that Saps Foods Inc. is any way related to what the Petitioner in this case does?

A Yes, I would say in some way it is related.

Q In what respect?

A Well, probably their primary raw material is probably -- is probably flour, wheat flour, so they have -- they are buying the same product, they are buying the same raw material as the subject company.

Q Well, does a bagel manufacturer use wheat, or a pretzel manufacturer, would you say therefore a pretzel manufacturer or a bagel manufacturer is similar to this taxpayer?

A I --

Q Even somewhat closely related? Is the operation of three restaurants, and the sale of things through vending

machines similar to this -- to what this taxpayer does?

A No, it is not.

Q Or even closely similar?

A No, each one of these comparables had some things that they do that are really not comparable at all to the -- to the subject --

Q Well, what does Sap's Foods do except use -- possibly use wheat, that is similar to what this taxpayer does? By this taxpayer, I mean Modern Maid Food Products, Inc. I'm waiting for an answer, I sat here waiting.

A Well, you asked me to express an area of comparability and I did express that as being the utilization of the same raw material, to me that is an area of comparability.

Q All right, let's take Bridgeford Foods, according to your record here, they distribute, manufacture, wholesale distribution of processed meats and delicatessen foods, that's their principal item. How was that related to what this taxpayer does, except that it is food?

A Of course, you only read part of the --

Q All right, the sale of fresh frozen smoked meats, and then as the fourth item, which I assume is listed in order of importance, the manufacture and sale of frozen bread dough products?

A Right, that of course is the area that has some comparability.

Q And to whom -- do you know to whom the frozen bread dough products are sold?

A No, I don't. We have already established that -- you know what I know about these comparables by reading the business thing.

Q The Manischewitz or Manischewitz, I have heard both pronunciations, on page 39 --

A Um-huh.

Q I guess they use wheat and matzos, matzo meal, farfel, cake meal, tam tam crackers, then we go to a little bit of different field, borscht, gefilte fish, baby foods, canned soups, Kosher sacremental wine, candies, and so forth. You mean the making of matzos, which is sold on the -- trucked to the stores for retail sale, that is the close relationship or the similarity with something that Modern Maid Food Products does?

A Well, it certainly is not a close relationship, I haven't pretended that it is. But, once again we have a similar raw material. Are we going to talk about Martha White Foods too?

Q Would you know how much the -- though you may have it, I don't know how much the net income sales from each phase of each activity of these companies I referred

A No, I don't.

Q Turning to your valuation on page 27, return on the net worth approach --

A Um-huh.

Q Assume the last earnings in balance sheet figures known are the close of a previous year, wouldn't a perspective purchaser be obliged to use those figures? In other words you have on page 27, the 1967 figures, and then you refer --

A Right.

Q On page 28 to 1968 figures, or using them as a guide, now assume for the moment, you don't know, though the testimony is that way in the Court, that there were no interim figures taken off, that the audit is made once a year, and the 1968 figures are known sometime in 1969. And, you have a prospective purchaser on August 21st, 1968, would he know any more than the figures of December 31st, 1967?

A No, of course not.

Q Then, in making an appraisal wouldn't you more or less have to use those figures, if the figures after that date are not known?

A If you are following your assumption, yes, that's right.

Q Only on my assumption, fine. Now, when one makes

a purchase, do you only look at securities stock of a closely held company, or any security, does one only look at the last year's earnings, or do they look at the year before and the year before, you know at least three years' earnings?

A Well, certainly they would look at as many prior year's earnings as they would have.

Q All right. And, wouldn't they be concerned to see if in those three years the earings were flat or the earnings showed an increasing trend?

A Yes, they would be.

Q And, it would be reflected in the market price, certainly, as a growth situation or a flat situation?

A Yes, that's right.

Q Mr. MacMullan, on page 30 of your report you have a series of ~~rotations~~, number and size of ~~rotation~~, number of ~~rotations~~, and the cost of ~~rotations~~, which is how you arrived at an 8 percent discount for going public. May I ask you where you obtained these figures?

A Yes, this was information that was made public by the Securities and Exchange Commission.

Q For 1968?

A No, I believe in fact these are considerably before 1968, prior to 1968, it would have been available to someone in 1968, however.

Q Well, are they 1967's?

A I'm really not sure, you know what year this relates to.

Q In other words this could relate to some year that has no bearing at all on the cost of going public --

A Well --

Q Have you recognized that there is a -- do you recognize --

MR. GOLDBERG: Your Honor, that's -- that's three questions in one.

THE COURT: Wait a minute.

MR. GELFAND: I think that he answered the other one.

(Pause.)

MR. GELFAND: I -- may I -- I thought that the Court was doing some calculations, are you waiting for me, I was waiting for you, Your Honor?

THE COURT: Yes, no, I'm waiting for you, Mr. Gelfand.

MR. GELFAND: Oh, I'm sorry.

THE COURT: I'm waiting for you, I was just doodling, that time.

MR. GELFAND: I'm sorry, Your Honor. There was a question, and I heard wait a minute, and that's it. All right.

BY MR. GELFAND: (Resuming)

Q Going back to my questions, do you know what year those figures of the SEC refer to?

A No, I am not sure what year they refer to, I am sure that they are prior to 1968.

Q Do you know, can you name any one company the size of Modern Maid that went public in 1968 or 1969 at a cost of 8 percent?

A You mean other than Modern Maid Company?

Q Other than Modern Maid?

A No, I can't.

Q Now, in these costs, is this just the underwriter's cost?

A Yes, that's correct.

Q Now, let's see what other costs, are there usually legal fees?

A Yeah, there are legal fees.

Q Accounting fees, special accounting fees?

A Yes there are. The bulk of the costs, however is the underwriting fee.

Q And, sometimes underwriters in addition to their initial charge get warrants, or buy cheap stock?

A Sometimes.

Q Sometimes. So those are all additional costs?

A Yes, however you will note that -- that the range

of costs that were available to me by this summary was 6 to 8 percent, and I used the higher figure than the 8 percent figure, maybe that offsets some of those additional costs that you are talking about.

Q That gets us to another phase. When one goes public, when a company goes public, is every single share sold, or is there a registration of some shares and the remaining shares, and some shares remain restricted?

A It -- it depends on the offering, it can be done both ways, certainly.

Q Well, every single share that the insiders hold is being marketed and sold out, aren't they in effect selling their company and withdrawing from it?

A I don't --

MR. GOLDBERG: Your Honor, is that a question or a conclusion?

MR. GELFAND: NO, with a raised voice, that's a question.

BY MR. GELFAND: (Resuming)

Q If every single share is registered and sold by the underwriter, aren't the insiders then selling their company?

A They are selling their stock in the company, certainly.

Q Is that how you are appraising this, that Mr. Silverman was selling his interest in the company?

A No, I'm not appraising it that way.

Q All right, let return to page 27, on page 27, you have an average for percentage of return of earnings to net worth of 12.89 percent and you used 13.0 percent.

A That's not correct.

Q That's not correct? What is your average then?

A You didn't say average, you said you had a return of 12.89 percent.

Q I'm sorry -- I'm sorry, an average return, I'm sorry

A Yes.

Q An average return on the net worth of 12.89, percent which is rounded out --

A Yes, I must point out that I also had a composite return of 13.77 percent.

Q But the 12.89 percent is the lower rate of return, so therefore 13 percent was taken, right. Let's -- now in that 12.89 percent you have an extremely low one, 6.94 percent, and one quite a bit above the others of 17.53 percent, Martha White?

A That's correct, yes.

Q All right. Where such a wide disparity exists, isn't it customary to eliminate the high and the low items?

A It is not customary, it can be done, it is an approach to things.

Q May I refer you to page 29, did you in that case have an average without the high and the low, and you used that one?

A Yes, I did.

Q All right, let's go to page -- 50, you have an average of 31, and an average without the high and low of 24, and didn't you use the one close to the 24, of 25 percent, which you said was the basis for your 25 percent?

A Yes, I did in that case, I think that in that case the high and the low are so far out of line, it is called for.

Q Well, isn't 17.53 and 6.94 out of line, isn't the 6.94 certainly out of line with the others?

A We are back on what, page 27?

Q Page 27.

(Pause.)

A Yes, I feel that they are out of line, however I feel -- you know that there is similar indication of percentage that's indicated by the composite and the average is my basis for using 13.0 percent.

Q Well, wouldn't you have that effect if one of the companies was weighted in the use of the figures that

it was so much greater than in others, that one could tend to offset the other? Isn't that actually what happened here? That the weighting of Martha White because of its size compensated for the extremely low figure on Manischewitz Company, and therefore your composite was what you consider almost the same? Actually if you eliminted the high and low, wouldn't you be closer to the composite, if you are saying that you are using the composite as a guide?

MR. GOLDBERG: Your Honor, Mr. Gelfand is in a narrative form asking so many questions in one, and it is just arguing with the witness as to the --

THE COURT: I think that most of what you are saying, Mr. Gelfand, could be very well taken care of in your brief.

MR. GOLDBERG: It is purely argumentative, Your Honor. It goes to the weight of the report.

BY MR. GELFAND: (Resuming)

Q Mr. --

THE COURT: I think that any witness called upon to do this type of job, why he is pretty much entitled to use any approach that he wants to, and then the reasonableness of his approach will be taken into consideration in determining the weight to be given to his testimony.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, have you made any calculations of what the figures would be on page 27 if you had used the composite percentage return?

A No, I haven't run through what those figures would be.

Q You said that you used 13 because it was pretty close to the composite, would you consider using the composite a fair basis too?

A No, obviously I feel that the 13 percent is -- is my estimate of a reasonable rate of return based on the comparables, and that's why I used it.

Q Why 13, in preference to 13.77?

A Because we have both -- we have two figures expressed here, 13.77 as a composite percentage return on net worth, and 12.89 as an average return -- percentage return on net worth, I used something in between the two, and it was actually closer to the average than it was the composite.

Q You did -- state that with respect to two other averaging you took the figures without the high and without the low?

A Yes, but neither of those did you have the opportunity to determine composite or average figures.

Q I believe that we have composite figures on page --

A I beg your pardon, I -- made an error in that, on page 29, you are looking for, there is a composite expression of the price earnings ratio.

Q Right.

A Of 17.9.

Q And, if we were -- all right, we'll pass on, leave it all for brief and calculation. On page 28, no page 29, I'm sorry, you have total value for each of your five selected companies, how did you determine these values?

A They were determined by a simple multiplication of the value of their shares times the total number of common shares outstanding.

Q And, is that listed on page --

A 33.

Q 33?

A Um-huh.

Q Now, this average price that you have listed, that's an average price of what?

A That's an average price of the stock for the year.

Q For the year?

A Yes.

Q You mean from January to December?

A Um-huh.

Q And, that's the figure that you take for August 31st -- August 21st to September 24th, on marketable securities?

A I believe so, let me just -- make sure that's what -- I have done here. Yes, that's what I have done because these -- these stocks were only traded in a limited manner, there is no way of determining the price of the stock on a given day, that far in the past, and they are not listed even in our over the counter exchange for example.

Q Well, let's take Bridgeford Foods, do you know what the range was for the year?

A I don't know, is it in the comparable section of the report?

Q It is on page 33, that Bridgeport Foods, one of your selected companies -- that is in the business of selling processed meats and delicatessen foods. Do you know what its range was for the year?

A No, I don't. I did know when I made the calculations, I don't know now.

Q I --

A Actually, Bridgeford Foods was offered, I think, it went public on -- or had a public offering or issuance on December 19th, 1968, at 8 3/4 a shares, and that is the figure that I used for that particular company.

Q Well, may I ask you to turn to page 41? How many common shares were there of Bridgeford Foods on November 1st, 1968? Outstanding?

A 600,101 shares.

Q And, October 31st, 1969?

A 704,301.

Q Didn't you determine that there was an offering of 100,000 shares, and that 4200 shares went to the underwriter, and that there was a public company owed during the year, you didn't determine that?

A I'm really not sure what your question is.

Q I'm asking you when you took these figures that there was a public offering in December the 19th, 1969, didn't you verify that that was only a public offering for 100,000 shares? And, that the other 4200 shares was then given to the underwriter as part of his compensation?

A Yes, I was aware of the size of the offering.

Q It was 100,000 shares?

A Un-huh.

Q And, there were 600,000 shares previously outstanding?

A Yes.

Q And,you didn't go to check what the market price was of that stock during the year -- even take an average as you did on the others?

A Well, in this case I thought that we had something that was better than an average we had a price that it was actually sold for at or near the dates of -- the as of dates of this report.

Q December 10th, is near August 21st, all right?

A It is not near August 21st, it is near December though, which is another one of our dates.

Q August 21st is the date of the gift, pardon me, did you know what dates the gifts were made?

A Yes, I understood that there were several gift dates that we are talking about here.

Q What gift dates have we got at issue in this proceeding?

A We have some in August, and September.

Q That's right. Do you believe that list of publically traded stocks vary, the market price varies from August to December?

A Yes, certainly.

Q Now, if that figure instead of 8 3/4 was some other figure like 6 or 5 or even 4, that would change all of your ratios and everything else, wouldn't it?

A If -- if in December of 1968 they went public at a price of 6 or 5 or 4, it would change my ratios, yes.

Q No, I said if on August 21st, where the average for the year was 4 or 5 or 6, that would change your whole

table and all your percentages, wouldn't it?

A You misunderstand, I had an opportunity to use an average for the year for that company, and I chose not to do it because I felt that the 8 3/4 price as evidenced by its sale in December of 1968 was better than the average for the year, and that's --

Q May I ask you why you thought it was better than the average for the year? Why should a price -- even if the average for the year is correct, why didn't you get the average for August, or the average for September?

A Because I was unable to find for these companies, the small size that they were, prices -- sale prices as of the given date of this particular valuation problem.

Q Are these over the counter traded securities?

A They were not at the time, no. Martha White may have been, the others were not, they are traded -- they are registered with banks and things like that, traded that way.

Q Have you ever heard of the expression pink sheets?

A Yes, I have.

Q All right, aren't securities of a number of companies that -- what should I say, that are not actively traded, aren't they listed in the pink sheets, bids --

A Yes, let's put it this way, when I say that they

are not traded over the counter, I meant that they are not listed on the over the counter market, and therefore you can't find by reading -- you know, the over the counter market --

Q You can't pick up the New York Times, and find it, --

A Right, it is infrequently traded stock.

Q But, aren't there still means of determining the price at which stock are being traded if they are not listed in the New York Times or the Wall Street Journal as listed over the counter stocks?

A Yes.

Q Aren't there means of finding out --

A Yes, there certainly are.

Q But, you didn't even do that in this case?

A The more current that the stocks are, the more near you are talking to this date today, the easier it is to do.

MR. GELFAND: Your Honor, may we have the record held open so that I could show, present to the Court what Bridgeford Foods was selling for, and show the effect on it in August and September?

THE COURT: You mean on the pink sheets?

MR. GELFAND: Or from the National Quotation --

THE COURT: Because if you do --

MR. GELFAND: Service.

THE COURT: I think that maybe we will have to have evidence to show just how that pink sheet was made up, and how reliable it was too, Mr. Gelfand.

MR. GELFAND: Well, what about from the National Quotation Service? There is a listing put out by the National --

THE COURT: We've had case after case in this Court, Mr. Gelfand, where at this time a lot of these prices were made by people selling to each other, and the Court would be inclined to agree with the witness that when he had a reliable public offering that was a lot better than the pink sheet. The pink sheet may have reflected some transactions in preparation for the public offering, I don't know.

MR. GELFAND: What about the fact that the public offering that sometimes the market is raised up just for the public offering and then it sells down again?

THE COURT: I say it may very well have reflected some transactions.

MR. GELFAND: All right, it works both ways, Your Honor.

THE COURT: That's right.

MR. GELFAND: Off the record, may I tell Your Honor a brief story about this? Hold it off the record,

please.

THE COURT: We have only a few minutes left on the tape, we'll give you another five minutes, how's that?

BY MR. GELFAND: (Resuming)

Q On the other figures that you have, average price for the year, where did you get that information? It is not from the New York Times, the Wall Street Journal and they are not active, that way, didn't you take them from the pink sheets?

A I took them from Moody's, which gives you a list of --

Q Where does Moody's get it from?

A I don't know where he gets it from.

Q In other words you just took Moody's figure without knowing whether it is right, wrong or otherwise?

MR .GOLDBERG: Your Honor --

THE WITNESS: Yes.

MR. GOLDBERG: That's purely argumentative, I would hope that Moody's would print rather accurate information because so many people are relying on their investment service.

MR. GELFAND: But if there is no daily market for it, Your Honor,then Moody's have no place of getting it but the pink sheets, unless we call Moody's in to show it.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, would you say that the dividend the company pays is a factor in the price earnings ratio?

A In the price earnings ratio?

Q Yes, what you call your P.E. ratio, market value compared to earnings?

A I would say that it is a factor indirectly in that it is certainly something that someone who is buying the stock would consider.

Q Do you know what dividends these -- your selected companies paid in 1968?

A Well, -- when you get into the area of dividends and the valuation of closely held stock, it is my feeling that the dividends are essentially a function of earnings and of net worth, and if you are going to consider them again, you are doubling up and considering something twice.

Q On page 33, comparable public enterprise approach, didn't you take into consideration earnings, net worth, and sales as three separate factors?

A Yes, I did.

Q All right. Now, when you compare each one to the market price, or total value, which is the market price times the number of shares outstanding, aren't you in effect giving consideration to the fact that a stock

paying a dividend, may sell at somewhat more than a stock not paying a dividend?

THE COURT: I think that may be your conclusion, not the witness's.

MR. GOLDBERG: Right.

MR. GELFAND: No, I'm asking him if --

THE COURT: Counsel, I mean take Eastman Kodak, or IBM, or -- these high multiples don't pay any dividends, do they, these rich fellows, -- rich tax lawyers like to buy those?

MR. GELFAND: These -- these companies aren't Eastman Kodak, American Telephone, I'm not talking about that, Your Honor, but when --

BY MR. GELFAND: (Resuming)

Q Let me ask him, hasn't a dividend any effect on the price earnings ratio of a stock?

A Well, you asked me that question once, and I said I feel that it has an indirect value, I'm not really sure how it would be measured, but --

Q All right, then I asked you did you know what dividends your selected companies were paying in 1968?

A I had that information available at one time, I don't know right now what it is, no.

Q You didn't play any part in your determination of fair market value, though, did it?

A No, it did not.

Q Would you please -- all right, on page 33, you have Sap's Food, with an average market price of 8, and you have Spaulding Bakeries with an average price of 8 1/4. Is that correct?

A Yes.

Q All right. Now, would you turn to your financial statements on each one, Sap's Food, is on page 42.

THE COURT: I think that we are going to have to recess at this point, and let the Reporter put a new tape in, so we'll recess until 11:30.

THE CLERK: All rise, please.

(Whereupon, the hearing in the above was recessed at 11:20 as described above.)

Tape 16 gv

BY MR. GELFAND: (Resuming)

Q I had suggested, Mr. MacMullan, that you turn to page 42, which list the financial data with respect to Sap's Foods, Inc. Now, am I correct your figures show that for the year ending May 31, 1967, this company earned $.49 a share and the next year $.71 a share, and the year ending May 31, 1969, $.90 a share?

A That's correct.

Q And, this company did not pay any dividends?

A That's correct.

Q Now, if we turn to Spaulding Bakeries, you

have the earnings for two years here, Spaulding Bakeries earnings are $.81 in 1968, and $.77 in 1969. In other words the same relative figures, but Spaulding Bakeries was paying a dividend, if my computation is correct of $.52 a share. In other words $218,000.00 on 420,000 shares in 1968, and in 1969. Is that correct?

A Yes.

Q $.52. So, the lack of growth in Spaulding as compared to Sap's Food was compensated by the dividends that Spaulding was paying and Sap's Food wasn't paying, if the market price is the same?

A That's your conclusion.

Q Well, what do you think it is?

A I think that that may be one of the factors that kept the price in the same area.

Q As an appraiser, would you say that Sap's Food would be worth -- the stock would be worth no more even if it paid a dividend, it wouldn't be selling any higher?

A As I have expressed before, the -- the contributory element of value to -- the -- that the dividend plays is really difficult to measure, and I have regarded -- I have considered dividends in this report, but I considered earnings and net worth basically, once you consider them, you have in effect considered dividends.

Q You are taking -- if you were considering earnings

to net worth only, I recognize that is a measure of the dividends, is compensated for a little bit by the fact that the dividends has reduced the net worth. But, you are also taking earnings to market price, and therefore --

A Um-huh.

Q And, therefore if a dividend has any affect on market price, the fact that one stock is paying a dividend --

MR. GOLDBERG: Your Honor, I object to this, this is purely argumentative, and should be brought out on the brief.

THE COURT: Objection sustained.

MR GELFAND: All right.

BY MR. GELFAND: (Resuming)

Q Let us go to page 33. In this -- on this schedule you have your first -- well, the third column from the right, you list earnings as a percentage of total value, and the total value is the market price times the total number of shares outstanding, is that correct?

A That's correct.

Q Now, doesn't the earnings as a percentage of total value reflect whatever factors are present in determining a market value?

A I don't think that I quite understand the question.

Q All right. Market value takes into consideration all of the factors that may exist that determines the market price of the stock?

A Yes, and one of those is earnings, is that what you are saying?

Q One of them is earnings, but when you take now, a percentage of earnings to market value, and the market values takes into consideration all the factors, that determine the market price when you finally get that percentage, as you have here 4.68 for Martha White, or 8.77 for Manischewitz, aren't you taking into consideration all of the factors that have affected market price of which the earnings figure is expressed as a percentage of?

A I still don't understand the question.

Q All right, let's try it again. Market --

A Well, don't just repeat it in the same way, because I don't think that I will ever understand it.

Q The market price takes into consideration all the factors, sales, net worth, earnings, dividends, whatever goes into -- growth factor, sponsorship, floating supply, whatever factors go into determining market price are reflected in the total value, is that right?

A Yes, that's right.

Q All right. Now, when you express earnings as

a percentage of that market price, you are getting a certain percentage that the earnings represent of -- of the market price or the total value where the total value already has all of the factors that affect the price in it.

A Well, maybe -- maybe -- maybe there is a misunderstanding as to what this percentage of total value really is, it is just step one in the mathematical step converting ultimately to a multiplier.

Q All right, it is column, one, two, three, four, five, six -- column six divided by column five, earnings divided by total value.

THE COURT: As the Court understands it, all it is is another way of expressing the price earnings ratio.

MR. GELFAND: The price earnings ratio.

THE COURT: That's all that it is.

BY MR. GELFAND: (Resuming)

Q And, in your net worth, you have got a price net worth ratio, and in your sales percentage you have got a price over sales ratio.

A Right.

Q All right. Now, if we were to take your composite figures, of 5.57 percent, total composite data, 40.50 percent and 170.92, and obtain the reciprocals, and divide

by three, and multiply each one times the base figure, earnings, net worth, and sales, we do come out with the 44 million, do we not?

A Yes, 44 million in total value?

Q In total value.

A Yes.

Q All right. Then, I would like to know why since each one of these factors represents the ratios to the total value, including all the factors that determine total value, why did you go and weigh one more than the other?

A Why did I weight earnings more than net worth and sales?

Q That's right.

A Because I felt that that's the most important factor in --

Q But your earnings are already expressed as a percentage of earnings value, in other words all the factors that go into market value are in there, each one is expressed as a percentage of the market value?

A There is a definite lack of understanding on my part on what point you are making now, I really don't follow this point.

Q You weighted --

THE COURT: Why don't we let the schedule speak

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for itself, Mr. Gelfand?

MR. GELFAND: All right.

THE COURT: The schedule shows what he has done.

BY MR GELFAND: (REsuming)

Q Didn't any question arise in your mind in your method of appraisal when you start with companies in quite different pursuits and your chart shows a variation of more than 2 to 1 in the price earnings ratio, of approximately 5 to 1 in the price net worth ratio, and 2 1/2 to 1 in the price sales ratio? In other words you have for Martha White on net worth a 26 percent return on market value, and in Manischewitz where the market price doesn't even equal the net worth of the company, doesn't any question arise regarding either the type of company selected or the method being used?

A Well, of course I wished that they were closer together, I wished they all were in a very tight bracket, it would be very nice. I think that we must realize that we are using more than one factor, we are using three factors, and if we consider that earnings, net worth and sales are some kind of contributory components of value, then we must realize that -- that a company that has for example lower earnings but a very high net worth, that high net worth might offset to some degree the lower earnings -- you know, that there is an interplay here, and you can't genera-

lize it in the way that you just have.

Q But, that's what I was trying to get when I asked you the first question, but isn't that interplay with respect to earnings already reflected when you take a percentage of earnings to the market value and the market value has all the other factors already in it? Isn't it --

MR. GOLDBERG: Your Honor, the witness hasn't answered the --

MR. GELFAND: All right.

THE COURT: Well, as the Court understands it, counsel, all counsel is saying is that the -- is that the price earnings ratio reflects risk, financial condition, and like that, I think that he has got in mind its current assets, and that undoubtedly is going to be reflected in the price, Martha White presumably has got a lot more seasoning, more established company, larger volume, and you expect probably a much more secure sales volume too for that matter. That's going -- everything is going to be reflected in the price earnings ratio, I would think.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, doesn't this chart consider what the different activities that the companies are in, isn't it really like taking pears, apples, bananas, pineapple, making a fruit salad, and comparing it to the one ingredient,

apples, because there is a single underlined thing, its fruit?

A Well, I think that I have really expressed myself as to what I feel, how valid the comparables are, you know, several times. And, it is just another way of asking me the same question.

Q Well, are you saying it doesn't or it does in answer to my question?

A Well, repeat your question --

MR. GELFAND: Please read it back.

(Whereupon, the reporter played back the portion requested.)

THE COURT: Let's answer the question in the affirmative, and get along here.

MR. GELFAND: All right.

THE COURT: I think Mr. Gelfand, that that's why the Court came back to the basic proposition that if you want to -- you want to get into the ultimate of the valuation study here, there are so many factors that are missing that the Court would be inclined to -- to entertain a motion that we strike all of them frankly. I think that the -- you don't do everything in every case. You could carry this company back a lot farther, I think, the longer the history the more -- the more reliable might be the projections. I think that you would have to tie it in with

economic indices, and somebody would have to project the future, and there so many things if you are going to use that type of approach, that you stop somewhere and accept the results subject to the qualifications, that if you wanted to use that Econometric Model up at Harvard, and spend $100,000.00, you might come up with another answer, but I'm not so sure that they would be any closer to being right than somebody else, they just over argue with what they do.

MR. MUSOFF: Your Honor, --

THE COURT: It's a sliderule game, when you get right down to it.

MR. MUSOFF: Your Honor, may I just make one or two comments?

THE COURT: Yes.

MR. MUSOFF: At the risk of ~~opposing~~ exposing my ignorance, I can't hold a candle either to the Court or Mr. Gelfand when it comes to statistics or anything of that nature, and it therefore seems to me that the thing that has most validity in these situations is the marketing concept, what something would actually sell for in the pragmatic scheme of life, and --

THE COURT: That's -- that's why I like the Ladenburg, Thalm report.

MR. MUSOFF: And --

THE COURT: That's closer to reality in the marketplace.

MR. MUSOFF: Except, Your Honor, that the whole situation changed by 1969. It would seem to me, that if I owned a company, Your Honor, and I'm no whiz as a readily admit when it comes to finance, but if I owned a company such as Mr. Jack Silverman owned, and I had an opportunity to unload non-voting shares and retain complete control of my company, it would seem to me that I would jump at the chance of selling it at 2 to $5.00 a share, because what am I doing, I'm getting -- it is better than going public. I'm still the sole manager of the assets. I'm retaining control, I don't have to answer to anybody. I don't have to get involved with the SEC, and it seems to me that pragmatically, if someone -- if -- like some investment banker came to me and said in your recapitalization, you have got so many thousands of shares of non-voting -- stock --

THE COURT: You can put that in your brief, but let me just point out one thing, you are talking about -- you are talking about,probably about what his annual salary was. There would be no point in selling what amounted to 40 percent of the underlying interest in the company for a year's salary, would there?

MR. GELFAND: It doesn't work out that way, Your

Honor, Mr. Silverman still had $1,370 -- let's see, $1,370,000.00 worth of preferred stock that was paying him a $5.00 dividend.

THE COURT: We can all work these figures out, but I say --

MR. GELFAND: You still --

THE COURT: Let's keep ourselves on -- on the question that we have before us now, and that is Mr. Gelfand's cross examination of which I think he is doing quite effectively, and it goes to the question as to how much weight -- what was the depth of the investigation let us say upon which this appraisal was based.

The witness frankly testified that he took Moody's and he flipped through Moody's and he picked what he thought was probably about as close a fruit to the apple as he could get, and he threw them all in the pot, and then he exercised his judgment, and he comes out with a figure. And, I think that one of the Petitioner's witnesses with a few variations followed the same approach, because when the -- when the American Appraisal figure witness got down to discounting, he didn't say why he discounted this one more or less than others, he had a range there, and he reaches out of the wild blue, and he pulls out a figure, and he says, I discount it this much.

But, I mean, all of that goes to the exercise of

judgment on the part of the witness now. We really have to accept all of these within those limitations.

MR. MUSOFF: Well, that's why, Your Honor, I am confused about why the marketing concept is not the more valid one --

THE COURT: Well, unfortunately we don't have the marketing concept before us, we didn't bring in Ladenburg, Thalm to tell us what they -- how they would have marketed 170,000 shares, or whatever it was of this stock, or whatever.

MR. GELFAND: As non-voting stock.

THE COURT: I know, I say that we didn't bring them in.

MR. GELFAND: Why is Ladenburg any more competent than Mr. Cannor or Mr. Wit?

MR. GOLDBERG: Your Honor, I --

THE COURT: Because I think that we would all assume that you try the market where you can get the most first.

MR. GOLDBERG: Your Honor, I think that Mr. Wit testified that he took purely the marketing -- the seller's -- the buyer's -- he would advise the buyer --

THE COURT: I say I --

MR. GOLDBERG: He wouldn't even consider what the seller would go for.

THE COURT: That's right.

MR. GOLDBERG: And, I think that here we are talking -- I think in these cases involving closely held corporations, there is nothing that is really comparable, the only thing that we have is the multiple of what the discount is, any other thing else --

THE COURT: It's a very -- it's a very difficult problem.

MR. MUSOFF: That's right, Your Honor, but back --

THE COURT: I think frankly if somebody had started with the -- with the price at which it went public, and worked back from there, it probably would have been a little bit more scientific than any approach I have heard so far, because there you have a point of reference to -- to go from. But, here you are starting from a platform that may or may not be right.

MR. MUSOFF: I understand that, Your Honor, but in 1968, things were different. The testimony of Mr. Silverman is that he at no time at that point ever thought of going public. He wanted to manage that company the way he did when he was 26 years old --

THE COURT: Well, when -- the last --the --the last gifts were made, when counsel?

MR. MUSOFF: September.

THE COURT: September of 1968, and when did the stock go public?

MR. GELFAND: October of 1969.

THE COURT: October of 1969. He had to have a change of mind fairly soon after that in order to go through the motions that you have to go through in order to go public, you don't do that in 30 days --

MR. GELFAND: I'm sorry for interrupting Your Honor, Mr. Silverman made his gift in August, so it is fully 14 months later when they went public, but the record is clear from the evidence that we presented that the first contact with Ladenburg was in March. In other words, and that was an incidence of needing funds that brought it up.

MR. MUSOFF: And, that was a result of his son bringing this idea to his mind. At that time, if you will recall, Your Honor, his testimony was that he intended to finance any expansion, not even by going to the banks, but to do this through internal financing, which is indicative of the operation of his mind. He started that business when he was 26 years of age, and he wanted to keep this his own business.

And, I think that this is the way that we have to look at it in 1968, and that's why I say, and maybe I'm taking a very simplistic approach, but it seems to me that

someone with this bent of mind would have jumped at the opportunity to unload non-voting stock to people that he would never have to answer to at something between $2.00 and $5.00 a share.

MR. GELFAND: And, he still has --

THE COURT: We can't put ourselves in Mr. Silverman's mind as of this time, but I might say very frankly, that I would believe that he would have sold that stock at that price at that time, and I think that he would have been out of his mind to have done so, because he would have gained absolutely nothing, and he might have picked up a nuisance as one of the witnesses testified to. I mean, I think that that is just a totally unrealistic assumption to make. And, the answer is, and there is nothing wrong with that, but Mr. Silverman would not have parted with the stock in 1969, except in the form of a gift. I don't think that we can ignore that.

MR. GOLDBERG: I think that in view of the fact that less than that, it was a matter of about 9 months --

THE COURT: But this is all good in the briefs, counsel, it will give you a good opportunity to write it in your briefs.

MR. GELFAND: All right. Your Honor, some of this goes to briefs, but I can't help -- pass one comment upon

the Court's remark about taking the market price and working backwards. That method was specifically rejected, in no uncertain terms by Judge Tannenwald in the case of Morris Messing --

THE COURT: Well, --

MR. GELFAND: That's 48 TC, 502. He said that there is no basis for taking such a thing. `It is a different picture, it is a different horse of another color. You are dealing with two different things.

THE COURT: Well, I -- I would be inclined to say --

MR. GELFAND: The Court may differ -- with Judge Tannenwald --

THE COURT: You have to limit each -- each case to what was presented. I -- I can tell you that I can go back a lot farther than that to 1939,and I can tell you that R. B. Mellons Estate was valued in precisely that manner, counsel. So, I mean it just depends upon how much money you want to spend and how far you have got to go.

I think that if you are going to take that, you are going to have to show -- cover the differences that occurred both in economic conditions, and in the -- in the attitudes of purchasers, and in other words you just can't pick one and say we subtract the increase in net worth in the interim, or something like that, it has to be done on

a -- on a very expert basis, and when you get all through, it is probably still a sliderule --

MR. GELFAND: That's true, Your Honor.

THE COURT: I used to go around during the Service, in a Captain's uniform renegotiating these companies, I mean it was absurb, when you got through, you got in the back room, and you took out your sliderule, that is about all you could do, you couldn't in the space of a few visits evaluate why one company should make X percent and another one another, it was an insuperable task. Well, we have pretty much the same type of job here.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, may I proceed with the cross examination, Your Honor?

THE COURT: Yes, sir.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, beginning with page 44, you listed a few court cases, did you select these as being representative of what you thought should be borne in mind?

A I selected those as the only ones that I found that -- that relate to discounts from fair market value for minority interests. These are all from a particular text book, McCarthy and Healy.

Q Did they guide you in any way?

A No, these did not guide me.

Q Then, why did you list these?

A I listed them for interest sake, really, they do relate to the -- they sort of substantiate the reasonability of the discounts that I took, I mean the discounts are within this framework.

Q Have you read these decisions?

A Yes, I have read them.

Q May I refer you to your Inga Bardahl on page 49?

A Surely.

Q In that case, didn't the Government's own expert discount 20 percent for the cost of floating the stock issue to the public, which the Court found to be acceptable?

A Yes, that is true.

Q And, didn't -- you didn't consider that any thought should be given to that figure?

A Well, I have already testified that I was not guided by the percentages in this case, neither the percentage discount for the lack of marketability --

Q No, I'm just talking about --

A I --

Q I'm sorry, I didn't mean to interrupt.

A No, I did not consider these percentages listed

in the Court cases as anything other than interesting evidence to substantiate that our total discounts were not unreasonable.

Q No, I meant the cost of going public, the financing costs of going public?

A What was your question?

Q Well, I said in this case, the Government's expert, and the Court found, or accepted that the discount for the cost of floating a stock issue to be 20 percent just for that factor. My question was, you didn't consider this determination at all in applying what discounts should be used for going public in the case of Modern Maid Food Products, Inc?

A No, I didn't. I would really have to question that 20 percent, I don't know where it came from.

Q I would like to turn to page 50, will you kindly explain how you arrived at the average of 31 percent -- for the minority interest discount -- indicated discount?

A I believe that it is an average of the figures -- percentage figures in the far right hand column.

Q Would you mind adding them up and dividing through?

A Sure.

(Pause.)

A Well, I see that they average 40 percent.

Q And, what is the average without the high and

the low?

(Pause.)

A I -- I preliminarily get 36 percent.

Q Before we get too startled with that discrepancy, let me turn your attention to the second item?

A All right.

Q LTV Electrosystems acquired Memcor, Inc?

A Correct.

Q And, as I understand it, they acquired the first 33 percent at a cost of $45,500.00 for one percent, and they acquired the next 67 percent at a cost of $88,100.00, may I suggest that the 97 percent is erroneous?

MR .GOLDBERG: What line is that?

MR. GELFAND: Line 2.

BY MR. GELFAND: (Resuming)

Q In other words, isn't the discount -- what has happened here is, I believe that the party who computed this took the $43,000.00 and took 43 on 45, instead of the discount being 43 on 88.

A I guess that's what happened, I don't know.

Q All right.

A And, the 97 percent is overstated there.

Q Well, anyway, accept my statement that that figure should be 52 percent, and the fourth item should be 50 percent.

A Um-huh.

Q And, the corrected averages of 28 percent, and the average without the high and the low is also 28 percent.

Now, I would like to go over the schedule with you. APO Corporation acquired U. S. Consumer Products, is that correct, is that what this is referring to?

A Yes.

Q And, LTV acquired Memcor and down the line the first company acquired the second company, is that correct?

A Right.

Q All right. The companies that were acquired, they are all either listed on the New York Stock Exchange, or they were on the American Exchange, or they have an actively publically traded market, isn't that correct?

A That's right.

Q All right. Are you -- is there any reason why you chose these companies, I mean certainly the acquisition by U. S. Smelting of Mueller Brass isn't similar is it?

A Isn't similar to what?

Q Oh, to the question of determining a minority interest for -- or a minority interest in Modern Maid Food Products, Inc?

A I don't think that the question of comparabilities is at issue here, I'm not saying that these are comparable in any way to the subject company --

Q Are these the only acquisitions that you could find for the year? Over the years, in fact it is not even the year 1968, is it?

A No, it is prior to 1968, it is information that would have been available to you in 1968.

Q Well, we are making an analysis today, don't you think that it would have been advisable to see what took place in 1968? I mean today we have the figures for 1968.

A Oh, you do have the figures for 1968?

Q Don't you think that in 1973 or 1974, we would have the figures for 1968?

A I'm unable to note any historical -- you know, correlation or change due to time in these particular two step acquisitions, I don't think that --

Q Well, if you were going to say no difference in time, take APO and U. S. Consumer Products, there there is a discount of 22 percent, and in Electro Systems which -- well, let's get one in 1968, Penzoil, the interest -- there was an interest acquired in 1968, a later date, that is about the only one that runs into 1968, we have a 50 percent discount. It says 98, but it should be 50.

A Yes, and you also have many of them in 1965 that are quite different too.

Q That's right.

A I really don't think that you can make any correlation between the dates --

Q All right, let's take any one of these. Well, let's take some generalities. You did say that these securities were publically traded securities on the -- listed on the exchanges, which were acquired by other large companies?

A Right.

Q All right. Were these acquisitions for cash or stock do you know, in other words when you used these values, this is a value of stock or in cash?

A I don't recall, I made the study quite awhile ago.

Q All right. When large blocks of publically traded securities are acquired, is it or is it not usual that they have some relation to the market price at the time?

A Yes, it certainly is.

Q All right. If the purchase and sale of a large block is crossed by one or two houses, do you know what I mean by a cross sale? No -- it is pretty close to the market price, is that right?

A Yes, that's right.

Q All right. But if some company is anxious to acquire an interest, it sometimes solicits tenders, and

then the market bid price can be quite a bit above the market price, I mean are you familiar with what has taken place at all in the last year, Grand Union's acquisition by another company, Air Reduction's acquisition of stock by British Oxygen Corporation, or any transaction --

MR. GOLDBERG: Your Honor, I don't know where this is getting. I have a feeling though that this schedule that Mr. Gelfand is referring to is merely historical data.

THE COURT: Well, --

MR .GELFAND: Your Honor, I can definite show, this goes to the heart -- he said he based his 25 percent discount on this schedule.

THE COURT: I think I -- I would like to be brutally frank at this point, and that is that the problem that Mr. Gelfand brings out with respect to the comparisons in this witness's report, I find the same problem exists with respect to the American Appraisal reports, so where does that leave us? That leaves us with two witnesses who said that they wouldn't have paid more than $6.00 or $2.00 a share. But, I'm not sure that that is sufficient proof of anything. They weren't the only buyers at this time, and they certainly didn't have any examples to where they had bought any stock, on that kind of a pricing, and maybe

that's all they would have paid, but there wouldn't have been any sellers at that price. So, I think that we are left with the -- I think that counsel for the Respondent said that he no longer is holding out for the $48.00 in the notice of deficiency, so we don't even have the presumption to fall back on.

I think that the Court will just have to take out my old sliderule, what I used as a renegotiator --

MR. MUSOFF: If Your Honor, please, we still have Mr. Cannon in the Courtroom, and in rebuttal we can put him on, and he can detail transactions that he was actually involved in during the year 1969?

THE COURT: I know, but counsel we are going to run into precisely the same problem, in that you are going to be comparing apples and oranges, and -- so that for every example that Mr. Cannon can give, I can probably give you an example of the peripheral computer field at this time, where the prices were absolutely incredible, see. So, I mean it is just --

MR. GELFAND: But crumbs --

THE COURT: He wasn't -- I'm sure that Mr. Cannon in 1969 wasn't interested in buying into the flour business at any price.

MR. MUSOFF: Well, --

THE COURT: Or 1968.

MR. MUSOFF: Mr. Cannon was in the business of making money, Your Honor.

THE COURT: That's right.

MR. MUSOFF: With his investments --

THE COURT: And, that's why he wasn't -- he is smiling, and I think that he agrees.

MR. MUSOFF: Do you think Your Honor, that a ten minute recess at this point --

THE COURT: Well, --

MR. MUSOFF: May we adjourn to chambers might be a better --

THE COURT: Yes, well, I was going to suggest to you that if the parties want, since we have a record here, if the parties so desire the Court will entertain a motion to -- to join the -- the case that is apparently pending for the subsequent year, and -- and we can have such further hearing as may be desired on that on the June calendar, but I just offer that as a suggestion. It just seems to me that it is going to be a lot easier if one Judge has both cases, because you have got all of the facts here.

MR. GELFAND: Well, Your Honor, I am not prepared to go with that case on the June calendar, we have just too many things --

THE COURT: Well, maybe I'll have this --

MR. GELFAND: That's why I wanted the continuation in --

THE COURT: Maybe I'll have the September one, Mr. Gelfand, -- let's -- well, we'll recess for a minute and go into chambers here and talk this over.

THE CLERK: Rise please.

(Whereupon, the hearing in the above was recessed at 12:15 as described above.)

BY MR. GELFAND: (Resuming)

Q I -- Mr. MacMullan, I believe that the last question that I asked that is if some company is anxious to acquire an interest, does it usually solicit tenders somewhat or even substantially above the market?

A I don't recall that being the last question, I answered affirmatively.

Q You answered that affirmatively, all right, I'm sorry, all right. And, after the purchse, the stock usually recedes to its previous trading range, is that right? In other words when someone makes a bid for some shares --

A Um-huh.

Q Usually bids above the market, acquires it --

MR. GOLDBERG: Your Honor, these are all generalities.

MR .GELFAND: No, I'm asking him a question.

THE COURT: No, maybe his going to test the witness's qualifications.

BY MR. GELFAND: (Resuming)

Q Does it then recede to the previous trading range?

A Not all the time, I would say frequently that does happen.

Q If --

THE COURT: I think that if there were any predictability in the market, Mr. Gelfand, you and I -- you and I wouldn't be here on this awful day --

MR. GELFAND: I wouldn't be here.

THE COURT: We'd be someplace else.

BY MR. GELFAND: (Resuming)

Q All right, let's turn to Penzoil's acquisition of United Gas. It acquired 42 percent in December, 1965, at a cost of $5,370,000.00 per one percent, is that right?

A Right.

Q And, in January of 1968, it acquired the -- it acquired the remaining 59 percent for $618,000,000.00 which was $10,660.00 per one percent, is that right?

A Well, the remaining 58 percent.

Q Well, the remaining 58, I'm sorry. It looks like 98, the remaining 58 percent. Now, that is two years, one month, or two years, two months later, isn't the price

that is paid in 19 -- two years apart dependent upon the market conditions at that time?

A Yes, it is. You have to remember that this -- that this particular transaction was one of the ones excluded through the use of throwing out the high and the low.

Q Well, except that when we correct it, it is no longer the high.

A Okay.

Q And, the figure in December, 1965 was dependent upon the market price at that time?

A Well, it would certainly be a close relationship to it.

Q A close relationship to it. So, the variation in percentages that you have here, are really determined to a great extent by the market price of the stocks at the different times they are bought, isn't that correct?

A That's partially correct, but remember that some of these two step acquisitions occurred fairly close together.

Q Well, I am asking you about the Penzoil, which is given in your general averages, giving you 1/6th weight, because you are eliminating the high and the low --

A Um-huh.

Q And, in -- ah -- let's see, Philadelphia

Reading's acquisition of Lone Star, there is a gap of eight months and the market does vary in eight months' time on publically traded stock.

Now, suppose somebody acquires a 92 percent interest when the stock is selling at 50, and finally buys the other 8 percent interest when the market is 60, so that we have a minority -- more paid for a minority interest than we did have for the majority interest, would you then say that a minority interest obtains a premium?

A No, I don't think -- that you -- you are making that conclusion, I --

Q No, -- no, this is based on the market values --

A Right.

Q I said supposing the market value had been such that at the time the minority interest is bought, the market price is much higher?

A Right.

Q We would then have a situation where the minority interests commanded a premium, isn't that correct?

A No, that is not correct. The minority interests didn't command a premium.

Q The market price --

A The market price changed.

Q Fine, well, to what extent have you given consideration to the market price fluctuations in the

determination of what discount is being allowed -- is really being paid for a minority interest?

A I haven't in this -- in this schedule I haven't made an attempt to adjust for that.

Q But your 25 percent was based upon that schedule?

A Yes, it is, it is an attempt frankly to -- to come up with some basis for -- for what a discount in minority interests might be, or to in the past I have seen people say that it is my opinion that it is this or that it is that, so this is an attempt to have a reason for an opinion.

Q I believe, Mr. MacMullan, that to a certain extent you equated non-voting shares with the minority interest?

A Well, I realized that the subject stock is a minority interest, yes.

Q And, that the stock is non-voting, are you saying that from your experience non-voting stock only sells at 5 percent less than voting stock?

A No, in fact, I used a 16 2/3rds percent discount.

Q Well, it is 16 2/3rds percent of the -- it is not 16 2/3rds percent of the market price, it is 16 2/3rds percent -- oh, it is $5.00 a share --

A Right.

Q Of an original price of $40.00 --

A No, we were at $30.00 at that point.

Q So you are saying that of non-voting stock you could get 5, 6 as much for non-voting stock as for voting stock in your opinion?

A No, that's not a completely accurate statement.

Q Well, what then does your 16 2/3rds discount --

A More -- more specifically that's my estimate of the difference in value between a minority number of shares in voting stock, and a minority number of shares in non-voting stock. And, it may seem like a fine distinction --

THE COURT: Let -- let's see if we -- let's see if we can't eliminate this schedule all together, because -- let's take U. S. Smelting, and Mueller Brass, would you agree that the situation as between U. S. Smelting and Mueller Brass would be something like General Foods buying Modern Maid?

THE WITNESS: Yes, I would, Your Honor.

THE COURT: In other words Mueller Brass used the raw materials that -- that U. S. Smelting produced. But, don't you have a situation where U. S. Smelting had already bought 82 percent, so that it is not like --

if U. S. Smelting was just going out and buying 18 percent alone. Isn't that right?

MR. GELFAND: Yes, that gives him 100 percent.

THE COURT: So, that whether they would pay more or less for 18 percent after they had obtained 82 percent is the real question. In other words, you really can't in the opinion of the Court, make any analogy between this type of situation, and the situation where if U. S. Smelting were just go out and buy a minority interest in Mueller Brass, what they might pay, nobody knows.

But, here you are just buying out minority stockholders, in a subsidiary, in which you already own the statutory requirement for consolidation. So, that -- ah -- in other words, if -- if Quaker Oats had already bought 82 percent of Modern Maid, then presumably this would be pertinent to show that they wouldn't pay as much as they paid for the 82 percent, but they would be willing to buy it at some discounted figure, isn't that right? Isn't that all that proves?

THE WITNESS: I don't know. As I said, Your Honor, I was attempting to find some basis for what --

THE COURT: I -- I -- I understand that, the question raised is, is whether or not there is sufficient analogy in that type of situation that it would have any meaning. And, I selected that one because I think that you

can probably at least draw a closer analogy than you can with respect to the others.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, if you were asked to appraise and determine the fair market value of an orange orchard, how would you determine that?

MR. GOLDBERG: Your Honor, I don't think that that has any relevancy here.

THE COURT: The objection is sustained. I wish you wouldn't remind me of it, the orange orchard business at this time.

MR. GELFAND: I like oranges, Your Honor.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, I would just like to call your attention to certain relationships and then ask you a question about it. The shares subject to gift represent -- that is the shares given by Mr. Jack Silverman, and Mr. Seymour Silverman, represent 70 percent of the total common stock. Though no one gift was more than 23 1/2 percent of the outstanding common stock.

To sell it as non-voting stock, Jack Silverman still kept more than 50 percent control, he had more than 50 percent of the A stock.

To value it as a minority interest in voting stock, Mr. Silverman's interest would drop to only 11.38

percent, of the total common stock, a totally different asset as far as the meaning to him.

In making one's appraisal, mustn't one actually appraise what is being transferred as the gift that keeps the same inherent character?

A I don't think that I ma going to flouder around and try to answer that question, I don't really know how to understand it.

Q Let me try again. Did you understand the first part?

A I understand your setting up of it, I don't understand the question itself.

Q All right. When you make an appraisal of what something would be based on going public and then working backwards, aren't you in effect making an appraisal that takes away from Mr. Silverman his control of the company, in other words he has more than 50 percent control when he makes a gift of non-voting stock, but when you take it -- well, it is public, and now I'm going to discount it back, you are giving him only 11.38 percent of the control of the company, aren't you really appraising then two different things?

MR. GOLDBERG: Your Honor, I believe that the American Appraisal Company discounted the total value of the company for going public also, first before they applied

the discount, which is the same -- you know, this is --

MR. GELFAND: I don't necessarily agree that that is a fair value, I think that that is too high, Your Honor.

THE COURT: Why don't you save all of this for your brief? I think that it is pretty clear from the witness's --

MR. GOLDBERG: I think that this is clear, Your Honor --

THE COURT: Report as to what the witness did, Mr. Gelfand.

MR. GELFAND: Well, I am asking him does he consider it -- in view of that does he still consider it proper, maybe he didn't think of it that way, I'm asking him a question does he still consider it proper to value something based on procedure that would take away from Jack Silverman his control of the company and bring it down to 11.38 percent?

THE COURT: Well, I don't think that anybody is valuing it on that basis.

MR.GOLDBERG: No.

MR. GELFAND: Well, when you value after it -- as if it went public and discounted it --

THE COURT: When I do it on that basis in my opinion, I'll be very careful to watch for that though.

MR. GELFAND: Objection, Your Honor, he is leading the witness.

THE COURT: Again, Mr. Goldberg, the objection is sustained, I think that -- that wouldn't the buyer want to know as much as he could, and the answer to that is yes. That's -- --

BY MR. GOLDBERG: (Resuming)

Q Mr. MacMullan, do you have a copy of --

THE COURT: The Court would like to know a lot more too.

BY MR. GOLDBERG: (Resuming)

Q A copy of the Prospectus in front of you?

A Yes, I have it here, somewhere.

Q I turn your attention to page 4?

A I haven't found my copy yet.

Q Okay.

A Okay.

Q I refer you to page 4, where we have the six months, ended June 30, 1968 unaudited?

A Right.

Q What is the net income at that point?

MR. GELFAND: Your Honor, I object there hasn't even been groundwork laid as to whether that information was available in August of 1968. Mr. Silverman --

THE COURT: Well, it was certainly available --

it was certainly available to the seller wasn't it?

MR. GELFAND: No, it wasn't, Your Honor. Mr. Silverman testified that no figures were taken off, this was made up sometime in 1969.

THE COURT: I know, but if you want to put Mr. Silverman back on the stand, fine, but I --

MR. GELFAND: He has already testified --

THE COURT: I think that you would be asking too much to ask the Court to assume that he didn't know how his business was doing month by month.

MR. GELFAND: I'm not saying that he didn't know --

THE COURT: Whether he kept it on the back of an envelope, or what he did, I feel quite sure that he wouldn't have been as successful as he was if he -- unless he knew exactly what was going on.

MR. GOLDBERG: And, I think a --- a buyer of this company would be entitled to know what the financial data would be.

THE COURT: Well, I think that when a man is going to make a substantial purchase, he is going to get an interim balance sheet, -- I don't think that there is any question about that, but the problem that we have here, Mr. Gelfand is, that when a man is going to make a gift, he is not going to go through the same type of

preparation perhaps as he would if he were going to make a sale. If Mr. Silverman was going to offer this stock for sale, I'm sure that he would have -- have an interim statement run off, isn't that right?

MR. GELFAND: Well, he would certainly know how the sales were progressing, Your Honor, but that's quite --

THE COURT: And, the buyer, he certainly wouldn't buy it unless -- unless he took the precaution of making sure that the business hadn't gone off the cliff since the end of the year, isn't that right?

MR. GELFAND: That's right.

MR. MUSOFF: If Your Honor, please, I have no problem accepting the Court's point of view in this regard, but for the interest of expediency, if it's just a question of reading what's already in some Exhibit perhaps we could do some rethinking here and shorten this trial process.

MR. GOLDBERG: It is only going to be another 5 minutes.

THE COURT: Pardon?

MR. GOLDBERG: It is only going to be another 5 minutes.

BY MR. GOLDBERG: (Resuming)

Q Based on that income for that six months period,

discounting -- subtracting from that the value of the preferred stock outstanding, what would the earnings be attributable to the common shares?

A As I work it out here, it would be, for the six month period it would be $2.83, a share.

Q And, would you project that on a yearly basis?

A Well, if a -- if a direct annualization is pertinent, it would be $5.66 a share.

Q Would you say that $5.16, would 10 times earnings be rather reasonable?

A Since I have already used 14 times earnings, I think 10 is conservative, yes.

Q Very conservative. Using 10 times, what would your value be?

A Well, the gross undiscounted value per share would then be $56.60.

Q And, what would you -- you have already testified that you used a 25 percent discount?

A I've used first of all an 8 percent discount for lack of marketability, a 25 percent discount for minority interest, and a 16 2/3rds percent discount for the fact that it was class B and non-voting.

Q What would your value -- can you --

A I can't do that in my head.

Q Would you work that out on a piece of paper for us?

A Um-huh.

(Pause.)

A All right, it is about $28.00 a share, a little bit more.

Q It is a little bit more than $28.00 a share.

A Yes.

MR. GOLDBERG: I have no further questions, Your Honor.

THE COURT: Mr. Gelfand?

RECROSS EXAMINATION BY

MR. GELFAND:

Q Your discounts that you referred to are discounts on the discounted figure, they are not discounts off the top figure are they?

A That's right, you have to make three multiplications here in order to get to that answer. You can't add up the discounts and do it once, you have to --

Q All right, now, when a company goes public, and you are looking at the Prospectus, as long as it is in evidence, were there large amounts of stock that remained unsold?

MR. GOLDBERG: Your Honor, this is purely --

THE COURT: Objection sustained.

MR. GOLDBERG: Away from the ground that I asked Mr. MacMullan just for a basic computation on the six month

figures on 1968.

THE COURT: Objection sustained.

MR. GELFAND: Well, I have no further questions on what he was asked on the redirect.

THE COURT: The witness may be excused.

(Witness excused.)

THE COURT: Did you say that you wanted to call Mr. Cannon back on rebuttal?

MR. GELFAND: I would Your Honor.

THE COURT: All right.

MR. GOLDBERG: Would you prefer after lunch or before lunch?

THE COURT: Pardon me?

MR. GELFAND: It is only five minutes -- I think that we would be all through the last of it even if I put Mr. Silverman back by 1:30 Your Honor, so I think that we ought to go and finish up. Mr. Cannon.

THE CLERK: Again, you are still under oath.

H E R B E R T C A N N O N, having been previously sworn, resumed the stand on the behalf of the Petitioner in rebuttal and testified as follows:

DIRECT EXAMINATION BY

MR. GELFAND:

Q Mr. Cannon, were you and the companies with whom you were associated making public offerings in 1968?

A Yes, sir.

Q Was it possible to float an issue similar to Modern Maid at a discount of 8 percent -- at a cost of 8 percent in 1968?

A To quote myself at one time, no way in Hell. If you want to know what average discounts were, for the cost of going public --

Q On -- on the -- about the size of Modern Maid?

A The NASD regulations at that time were permitting the total cost of going public up to a maximum of 25 percent. They have since reduced that now to about 18 percent. The actual cost though in practice, of course, the very very tiny little Reg A (phonetics) might run this high, but a company of this size, an issue of this size would normally run anywheres from a 7 to a 10 percent commission according to who the underwriter was. Most of the times I would say 8 to 8 1/2 percent to narrow it even finer. You would have about a 2 to 3 percent cost factor for accounting, legals, up to maybe 3 percent including printing. Most of the time you have an expense factor for the underwriter on top of his commission of another 1 or 2 percent, and in many many cases, there is also in this case, there would be warrants granted to the underwriter to purchase stock at usually 20 percent above the issue price over a 5 or 6 year period.

The NASD would give an evaluation to that, at approximately 2 1/2 percent of total value. So, on an average I would say that your total cost would come to about 15 percent as the issue got bigger it got down to 13 percent, and maybe 11 or 12, once it got very substantial.

THE COURT: Let me interrupt for a minute, those warrants though you didn't take into income at the time that you received them, did you?

THE WITNESS: The underwriter?

THE COURT: Yes.

THE WITNESS: We would not take them into income because they are exercisable only to 20 percent over market, if he got cheap stock he would have to take it into income.

THE COURT: So, that actually -- how can you say that that is a cost of the issue?

THE WITNESS: I quoted the NASD evaluation in terms of determining what they consider maximum cost factor.

THE COURT: No, but I mean, how does that -- how does that cost the issue or anything?

THE WITNESS: Well, according to the NASD they figure that eventually --

THE COURT: I'm not talking about the NASD, I'm just talking about --

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THE WITNESS: All right, as a cost factor to the issuer, he being optimistic is going to assume that the stock is going to go up over the period of years, which -- of which the warrants can be exercised, and therefore when they are exercised, and let's say that the stock has doubled or tripled, he is giving it away at a 50 percent or 100 percent discount, and therefore it is a definite cost factor to him, because it has a value. And, the fact that it has a value is why so many underwriters fight like heck to get them.

Now, how he treats that taxwise is out of my field, but it is a definite considered cost factor to him.

BY MR. GELFAND: (Resuming)

Q Was your -- were you or your company with which you were connected instrumental in bringing out any issues, or trying to bring out any issues in 1968, having to do with ingredients that used wheat?

A I -- I don't recall any.

Q Field's Baking Company?

A Well, Field's Baking Company, I have been a consultant to on and off over the years, is in the baking business, they make bread under their own label, and under the Grossinger label. We were attempting to either sell them into a public company during those years, or perhaps by control of a public company, but we didn't consider

taking them public, or they weren't interested in it either.

Q Oh, I see. What price was going -- were you trying to obtain for merging it into having it acquired by or acquire another company, I mean you could work it as a downstairs acquisition, or -- which I say, have someone else buy you, what price was attempted to be obtained?

A Management would have been very happy to get 8 times earnings at that time in terms of a full fledged substantial public vehicle.

They were doing about $6,000,000.00 in sales, which may be germane to the terms of comparisons in that time, and were making fairly good money, I don't recall exactly, but I believe it was around $500,000.00 they were showing pre-tax at that time.

They were offered a deal of about 5 or 5 1/2 times earnings as I recall, and did turn it down, and we never could get them one at about 8 times earnings. We tried at one time to buy a public company that was in the baking business, whose name I can't seem to find, but it was up around Rochester or Albany, and the estate which controlled that stock was entertaining a sale at 7 times earnings, but we couldn't finalize it because management insisted on buying a substantial piece of the company

itself, and they had to -- based on the continuity of the business, sell it to management, so we were never able to finish that deal.

Q This reference to Field's Baking and the effort to sell it somewhere, they got an offer of 5 1/2, and they wanted 8 and they couldn't get that, what year was that?

A The the area, around 1969, it might have been late 1968, the beginning of 1969.

Q Mr. Cannon, you were in Court when Mr. Mac'Mullan testified, I mean you heard all his testimony?

A Yes, sir.

Q Are there any comments that you wish to make on any specific phase of it that is knowledgeable in your particular field of things?

A Well, that's a large question. I think that his basic approach as I guess it would be on his side of the fence would be an extremely liberal one. To talk about net worth and price earnings ratio, and give value factors to both, and add it in, I think is a little bit over liberal from the way that I look at it.

Of course, being in the stock market, we basically consider price earnings ratio, and of course liquidity in terms of purchase. Most of his discussion was given on the basis of a publically traded stock with a small discount of 25 percent. Now, that I can't agree with the basic

premise there, because I don't think that anybody at any time, even in the throes of 1968 when everybody had money to burn was buying private stock without a right of registration at only 25 percent discount. Even then they were being generous with maybe a 50 percent discount, in several cases.

As I testified a few minutes ago, in his evaluation of an 8 percent cost factor for going public, I think that he is totally out of line. The only 8 percent factors that I have ever seen are in the utility issues, where you are putting out $50,000,000.00 and you can do it at a 6 percent commission. Your expense factor is very small because of the total volume of the deal.

So, I can't go along with his basic premises to start with.

Q Are you familiar with the Value Line Development Capital Corporation or the Value Line?

A Yes, I have had certain dealings with them, and sold them securities.

Q I wonder if you could explain this a little more, I mean have you had personal contact with them?

A Yes, I know Dr. Bernhard who runs the Value Line Fund, and have had dealings with their analysts.

Q All right, there is a statement in here on page 18 of the report of the American Appraisal Company, Value

Line has stated that it is a policy that at lesat 50 percent of the valus of restricted securities of its portfolio must be the subject of a commitment on the issuer to register at VAlue Line's request the securities under the Securities Act of 1933.

Now, are they saying that they -- what this at least 50 percent, would you know from your experience what percent of the securities --

A I believe that that was taken in the context of them going into an offering circular, or Prospectus to raise additional money or monies for some of their funds. And, to use an analogy, if you were going to create a corporation, you would give yourself as much latitude and ability to do things as possible.

Well, the maximum latitude that you could give yourself as a public entity buying securities would be to say to a potential investor that I will never invest more than 50 percent of your money in a security under which I have not got the right of registration. As a practical matter, and Dr. Bernhard and his people being rather practical, I don't think that there was any way where they would ever entertain in their minds, the fact that they might even come near 50 percent of their total dollars in securities without rights of registration. As a matter of fact, I think that they never invested more than maybe ten or 15

percent in those heydays.

Q I am really not familiar with your expertise, as it applies to what the previous witness said, if you have anything else that you would like to comment with respect to his analysis?

A Well, the -- I don't know whether it is in respect to his analysis, or -- what you both referred to before in terms of what you would pay or put up for private stock, now I participated or negotiated and completed five or six or seven private placements during the years in question, of 1967, 1968, and 1969. And, if it would be any help in terms of reviewing any of those, I can tell you what -- what we did in relation to book, and in relation to market, though they were not in the baking or flour industry.

THE COURT: I don't think that those would be pertinent, Mr. Gelfand. As a matter of fact, I think that I could ask the witness two or three questions here that would demonstrate that. Now, you are familiar with several of the -- you must know that there are several investment houses that place foreign funds over here, isn't that right?

THE WITNESS: Yes.

THE COURT: Isn't it true that they will come over here, and not only buy a minority interest, but they'll trustee the loading of a minority interest?

THE WITNESS: It's -- yeah they do that, it is a question of who is giving the trust to them, relying --

THE COURT: And, and they give it to a bank or somebody, --

THE WITNESS: Heavily on the investment banker, --

THE COURT: Right.

THE WITNESS: Right, the investment banker they are relying on most of the time.

THE COURT: And, also they will do it, they will do it without any commitment as to listing, won't they?

THE WITNESS: No, most of the time I have found that they will require a right of registration at somewheres down the pike.

There are cases, of course, where they haven't, but I would say that --

THE COURT: In other words, isn't it more important really to size up whether or not the Hon. Tripplin Moore, (phonetics), is the kind of a fellow that wants to make money, and he is going to want to list anyway, the right of listing doesn't do much good if the stuff isn't marketable, is it?

THE WITNESS: Well, when you say listing --

THE COURT: In other words, the -- the -- the attractiveness of the venture is much more important than

whether or not you could list it, isn't that right?

THE WITNESS: I disagree with that. The attractiveness, -- the event of the investment is the prime question before you invest a nickel, but the ability to dispose of it is also a very strong second question.

THE COURT: But -- you are telling -- yes, but if you are going to list a dog, what good does the listing do you?

THE WITNESS: I agree with that, I wouldn't buy it.

THE COURT: Okay, that's what I meant.

THE WITNESS: Oh, yeah, if it is no good, it is no good no matter what your rights are.

THE COURT: That's right.

THE WITNESS: And, of little value. In terms of --

THE COURT: Now, one more question, isn't it true, or am I wrong, that this type of business wasn't the type of business that would attract the so-called venture capital anyway?

THE WITNESS: No, I was very surprised to see that the Ladenburg did this deal, I think that they did it because of a moral commitment, and --

THE COURT: Well, I think that it is something else to sell it on the outside, but I mean if you were

trying to make a private placement with some of these so called venture capital people, and -- well, there is Rusell (phonetics), I think that they do a lot today, don't they, and --

THE WITNESS: Well, there are plenty around, more so --

THE COURT: And Paine-Webber (phonetics), don't they have that group up in Boston that do quite a bit?

THE WITNESS: Well, a little bit.

THE COURT: But they are not attracted to this type of business, are they?

THE WITNESS: They wouldn't really be attracted to this type of business, because number one, it is not considered a fabulous growth industry, which is what everybody was looking for in 1968.

THE COURT: All right.

THE WITNESS: And, it had flatness of earnings, two reasons to probably knock it out of the box, to be considered.

THE COURT: They are not interested in the food business,are they?

THE WITNESS: Only if they can get it at a real bargain, you know, as I stated in my own testimony.

THE COURT: All right, Mr. Gelfand?

MR. GELFAND: No further questions, Your Honor.

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Cannon - direct rebuttal

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THE WITNESS: I just wanted to add one thing further --

MR. GELFAND: One thing --

THE WITNESS: That you asked me to clarify that I forgot for the record, in terms -- there was reference made to Moody's and reference made to the pink sheets.

BY MR. GELFAND: (Resuming)

Q Yes.

A Well, the pink sheets are a very qualified way prior to Nazdec (phonetics), which there is today, way of determining the marketability of securities. Of course the more brokerage making market in the stock, the more valid you would have -- the validity would have in terms of selling a substantial amount of shares. But, Moody's themselves, take all their prices out of the NASD quotation sheets, National Quotation Bureau sets it. The fact that it is not listed in the newspapers is only a matter of two considerations, which the Times and the Journal have had over the years. Number one, the amount of shares in the hands of the public, and a minimum amount of States in the United States, today being about 30, I think that they require. And, the amount of shares in the public float, and it has nothing really to do with earnings, and it has nothing to do with book value of a corporation. It is just a question of how many people might pick up a newspaper and

pay the dime so that they can read the price of it. And, they go by distribution factors strictly.

Q What was the name of this, you said National Quotation?

A National Quotation Bureau is responsible for the pink sheets.

Q Oh, those are the pink sheets?

A Those are the pink sheets, that's the manufacturing company --

Q And, Moody's gets their information from these pink sheets?

A In terms of what goes into their nice big fat blue book, yes, in terms of price ranges.

Q Thank you, Mr. Cannon.

MR. GOLDBERG: I have some questions.

THE COURT: Thank you, Mr. Cannon.

MR. GOLDBERG: Just a couple questions.

CROSS EXAMINATION BY

MR. GOLDBERG:

Q Mr. Cannon, are you aware that the company was encapitalized in 1969?

A Was recapitalized?

Q Yes.

A Yes, sir.

Q And, there was one class of stock issued?

THE CLERK: Rise please.

(Whereupon, the hearing in the above was recessed at 1:30 as described above.)

Tape 17
22
3-29-74

THE CLERK: You are still under oath, Mr. Silverman.

J A C K S I L V E R M A N, having previously been sworn, resumed the stand on the behalf of the Petitioner on rebuttal and testified as follows:

DIRECT EXAMINATION, REBUTTAL, BY

MR. GELFAND:

Q Mr. Silverman, I want to refer back to the reorganization that took place in June of 1969, it may be that I heard incorrectly, I am not sure what your answer was, but I fear that I may have heard incorrectly, I want to go over something.

The reorganization in 1969, the terms of it, who suggested that? The second reorganization?

A The recapitalization was suggested by Ladneburg, Thal[illegible]

Q I mean that wasn't one that your organization decided before that?

A No, this was done in 1969, by Ladenburg.

Q I'm sorry, I didn't mean to interrupt. The recapitalization in 1969 was done by whom -- the terms of it was done by whom?

A The terms of it were done by Ladenburg, Thalmann. They were the underwriters.

Q They wanted to make a marketable situation?

A That is right.

Q The sale of stock was made to the employees in August, September of 1968, was that in any way related to their earnings?

A No, sir.

Q The amount that they took, was that in any way related to their earnings or position or anything?

A No, it had no relation whatsoever.

Q Was it based just on how much they wanted or could afford to pay?

A We selected the key employees, and associates, and we asked each individual how much they would want, and what they could afford to pay.

Q Thank you, no further questions.

CROSS EXAMINATION BY

MR. GOLDBERG:

Q On the 1969 recapitalization, the underwriters made the decision on the ratio?

A They did.

Q Did they talk to you about it?

A They did.

Q Did you agree to it?

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UNITED STATES TAX COURT

SEYMOUR SILVERMAN, ET AL,	)	
	)	
Petitioners,	)	Docket Nos. 3707-72
	)	3708-72
v.	)	3709-72
	)	3710-72
COMMISSIONER OF INTERNAL REVENUE,	)	
	)	
Respondent.	)	

BRIEF FOR PETITIONERS

PRELIMINARY STATEMENT

These cases, involve the following deficiencies in gift taxes asserted against petitioners for the calendar year 1968:

Seymour Silverman	$116,902.50
Helen Silverman	116,902.50
Jack Silverman	259,087.20
Frances Silverman	259,087.20

Petitioners now contend they have overpaid their gift taxes as follows:

Seymour Silverman	$ 11,646.50
Helen Silverman	11,646.50
Jack Silverman	28,776.00
Frances Silverman	28,776.00

These cases were consolidated for purposes of trial, filing briefs and opinion pursuant to a joint motion granted by the Court on March 27, 1974.

PETITIONERS' REQUESTED FINDINGS OF FACT

Petitioners respectfully request the Court to find the following facts:

1. Modern Maid Food Products, Inc. was organized on January 7, 1952 as a successor to a partnership formed in 1933. It has engaged in the business of manufacturing and selling breadings and batter mixes for use by processors of shrimp, fish and poultry, and the manufacture and sale of prepared flour mixes to which only water need be added for mass feeding outlets such as hospitals, restaurants and hotels. The flour mixes are sold through wholesale grocers (Stip. 3, Tr. 11, 33, 34).

2. On April 22, 1968 Modern Maid Food Products, Inc. requested a ruling from the Commissioner of Internal Revenue with respect to a proposed reorganization. The purpose of said reorganization was to solidify the employment of key personnel by offering to sell them non-voting common stock in the company and obtain some fixed return on investment for major stockholders (Tr. 9, 10, Ex 5-E).

3. On June 28, 1968 the Commissioner of Internal Revenue issued his ruling to the request made on April 22, 1968 (Stip. 5).

4. On August 11, 1968 the outstanding shares of capital stock of Modern Maid Food Products, Inc. were held as follows:

	Common Stock $100 Par Value	Preferred Stock $100 Par Value
Jack Silverman	1,284	265
Seymour Silverman	645	430
Harold Oppenheim	225	150
Stanley Silverman	3	10
Jack Silverman	3	10
Jack Silverman Foundation		575
	2,160	1,440

(Stip. 6)

5. Modern Maid Food Products, Inc. voted to adopt the proposed plan of reorganization on July 13, 1968 which became effective on August 12, 1968. On that date the outstanding shares of capital stock of Modern Maid Food Products, Inc. were held as follows:

	Class A Common $10 Par Value	Class B Common $10 Par Value	5% Cumulative Preferred Stock $100 Par Value
Jack Silverman	12,840	51,360	14,389
Seymour Silverman	6,450	25,800	7,525
Harold Oppenheim	2,250	9,000	2,625
Stanley Silverman	30	120	43
Joel Silverman	30	120	43
Jack Silverman Foundation			575
	21,600	86,400	25,200

(Stip. 7)

6. Gifts of Class B Common stock of Modern Maid Food Products, Inc. were made as follows:

Date	Donor	Donee	No. of Shares
8/21/68	Jack Silverman	Trust for Benefit of Joel Silverman	25,680
		Trust for Benefit of Stanley Silverman	25,680
9/24/68	Seymour Silverman	Trust for Benefit of Susan Silverman	8,600
		Trust for Benefit of Anne Silverman	8,600
		Trust for Benefit of Beth Silverman	8,600
12/8/68	Harold Oppenheim	Martin Oppenheim	2,000
		Sandra Oppenheim	2,000
		Trust for Benefit of Elysia Beth Oppenheim	2,000
		Trust for Benefit of Robert Alan Oppenheim	2,000

(Stip. 11)

7. Modern Maid Food Products, Inc. made the following sale of original issue Class B common stock in September 1968 at $10 per share, pursuant to agreement made on August 12, 1968:

Name	No. of Shares	Position	Approximate 1968 Remuneration
Hercules Adams	200	Salesman	$28,000
Ron Bronsweig	200	Plant Manager	17,000
Tony Cimorelli	200	Asst. Maintenance Manager	11,500
Latif Elias	100	Salesman	33,000
Robert Fussell	100	Salesman	31,000
Joshua Hoffman	200	Outside Management Consultant	
Arthur Jaspan	90	Member of Law Firm	
Joseph Jaspan	400	Member of Law Firm	
William Lipton	200	Salesman	50,000
Martin Luck	400	Salesman	28,000
Minnie Miller	300	Bookkeeper	9,500
Michael Piccirillo	400	Foreman - Maintenance	19,000
Eddie Soregaroli	400	Production Foreman	12,000
Joe Silverman	800	Traffic Manager	17,000
Neil Trager	200	Head of Research Lab.	12,000
Arthur Ulman	200	Salesman	20,000
John Urban	400	Vice President - Processing Div.	26,000

(Stip. 12, Ex. 14-N)

8. The offer of Modern Maid Food Products, Inc. Class B common stock to employees at $10 a share was not intended as compensation nor did the Corporation claim any deduction for any possible value in excess of $10 a share on its tax return (Tr. 10). The number of shares of class B stock sold to employees was not related to their compensation or position, but the selected employees bought what they could afford (Tr. 245).

9. The $10 a share value set by the Corporation was based upon book value of Modern Maid Food Products, Inc. and the fact there were no dividends on the new common stock.

(Tr. 10)

10. Jack Silverman and Seymour Silverman filed U.S. Gift Tax returns for the calendar year 1968 in which the Class B common stock of Modern Maid Food Products, Inc. was valued at $10 a share. Frances Silverman and Helen Silverman, spouses of Jack and Seymour respectively, consented to have the gifts made by their husbands during the calendar year 1968 considered as having been made one-half by them (Stip. 1 and 2)

11. Jack Silverman was 61 years old and president of Modern Maid Food Products, Inc. in August 1968. (Tr. 8, 9, 30)

12. Dividends paid by Modern Maid Food Products Inc. in 1964 through 1968 were as follows:

Date	Preferred	Common
1964		
April	900	
June	900	
Sept.	900	18,000
Dec.	900	
	3,600	18,000
1965		
March	1,800	
June	1,800	
Sept.	1,800	28,800
Dec.	1,800	
	7,200	28,800
1966		
April	1,800	
July	1,800	
Oct.	1,800	36,000
Dec.	1,800	
	7,200	36,000

1967		
April	1,800	
June	1,800	
Sept.	1,800	
Nov.		37,800
	5,400	37,800
1968		
Feb.	1,800	
April	1,800	
June	1,800	
Sept.	12,492	
Dec.	31,500	
	49,392	-0-

(Stip. 13, Ex. 10-J)

13. No dividends have been paid on the common stock of Modern Maid Food Products, Inc. after December 31, 1967. (Tr. 25, 26, 123)

14. The pro-forma book value per common share of Modern Maid Food Products, Inc. at December 31, 1967 was approximately $10 a share non-consolidated and $12. a share on a consolidated basis. (Ex 7-G) [($3,579,000 - $2,520,000) ÷ 108,000] and (Ex 8-H) [(3,851,000 - $2,520,000) ÷ 108,000]

15. Consolidated operations of Modern Maid Food Products, Inc. and subsidiaries for the calendar years 1964 through 1967 reflect the following:

	1964	1965	1966	1967
Net Sales	$8,255,805	$9,711,555	$10,673,769	$11,739,411
Cost of Sales	5,291,198	6,291,795	7,162,996	7,709,696
Gross Profit	2,964,607	3,479,760	3,510,773	4,029,715
Selling, General and Administrative Expenses	2,105,095	2,300,100	2,413,066	2,788,565
Income From Operations	859,512	1,179,660	1,097,707	124,150
Other Income (Deductions)	(3,401)	15,424	29,664	43,244
Income Before Income Taxes	856,111	1,195,084	1,127,371	1,284,394
Federal, State and Local Income Taxes	430,364	572,602	538,148	648,733
Net Income	425,747	622,482	589,223	635,661

(Stip. 10, Ex. 9-I)

16. The earnings of Modern Maid Food Products, Inc. in 1965 through 1967, the three years preceding the gifts at issue were "flat", the deviation from the mean being 3% on the upside and 6% on the downside. (Ex. 9-I, Ex. 19, p. 6)

17. The Class B common stock of Modern Maid Food Products, Inc. sold to employees was subject to a buy-back agreement under certain circumstances and in the event of death and termination of employment (Ex. 14-N) The buy-back price was the book value of Modern Maid Food Products, Inc. reflected in the last Federal income tax return. (Ex. 14-M) Modern Maid Food Products, Inc. filed separate (non-consolidated) income tax returns.

18. There was no buy back agreement with respect to the Class B stock that was the subject of the gifts at issue. (Tr. 12, 124)

19. Competitors of Modern Maid Food Products Inc. in the prepared flour mix division were Pillsbury Flour Mills, General Mills and DCA Food Industries; competitors in the breading and batter division were Newlywed Baking Co. of Chicago, DCA Food Industries and Griffith Laboratories of Toronto, Canada (Tr. 12)

20. Class B stock had no right to representation on the Board of Directors, no right to a voice in management, business policy or declaration of dividends. (Tr. 12, Ex. 13-M)

21. Up to and including the dates of gifts of Class B common stock of Modern Maid Food Products, Inc. there were no negotiations or agreements for the public sales of any securities of the Corporation or for the merger or sale of Modern Maid Food Products, Inc. (Tr. 13)

22. Up to and including the time of the gifts, Jack Silverman had no intention for Modern Maid Food Products, Inc. to become publicly owned or to merge or sell the Corporation. (Tr. 13)

23. During the summer of 1968 there was no dramatic change in the nature of operation of Modern Maid Food Products, Inc. as the result of any invention, new process, product or acquisition. (Tr. 13)

24. Modern Maid Food Products, Inc. became a "publicly owned" Corporation on October 28, 1969 more than 14 and 13 months after the dates of gifts by Jack Silverman and Seymour Silverman, respectively. (Tr. 13, 27, Ex.P)

25. In the latter part of 1968, Modern Maid Food Products, Inc. received an unsolicited inquiry about a possible expansion program in Canada. Such a program as well as other expansion plans caused a need for additional funds. Modern Maid Food Products, Inc. did not seek to "go public", but in discussing financing problems, Jack Silverman's son, Stanley, an employee of the company, was brought ultimately together with the underwriter. The first negotiations with any underwriter was in March 1969 (Tr. 13-15, 36, 41, Ex. 15).

26. The last financial statement of Modern Maid Food Products, Inc. up to August 21, 1968 was the one of December 31, 1967. There were no interim audit figures. (Tr. 38)

27. Petitioners presented three expert witnesses: The first was Harold Wit who is the executive vice president and Director of Allen and Co., Inc., investment bankers, and a member of its executive committee. Mr. Wit has been with Allen and Co. since 1960. Prior to that he was Vice-president and secretary of One William St. Fund, a mutual fund managed by Lehman Bros. (Ex. 17, p. 1)

28. With Allen & Co., Inc. Mr. Wit was engaged in investigating investment opportunities for that company to invest its funds in private and public situations. He has been involved in mergers, acquisitions, pricing of public and private sales and purchases of securities. He is responsible for reviewing and passing upon public and private financial transactions up for decision with Allen & Co., Inc. He has looked at and reviewed approximately three situations a week for the past 13 to 14 years. These situations ran the gamut of investment opportunities and involved origination, investigation, evaluation, negotiation, closing and monitoring. (Ex. 17, pp. 1 & 2)

29. Harold Wit's appraisal was based upon his expert judgment of what a knowledgeable buyer would be willing to pay for a substantial block of Class B common stock in the light of no say in Company affairs and non-liquidity of the investment once made. He considered the purchase of such ~~sauch~~ shares to be a rank speculation that some day in some way something would happen (a possible public offering or a merger) to increase the value of the investment. Under such circumstances, depending solely on uncontrollable happenstance, a purchaser would seek to realize $10 for each $1 invested. Until such hoped for realization, the purchaser could expect nothing - no dividends, no salary or other compensation. Based upon an ultimate possible market value of $50 to $60 for a Class B share, Mr. Wit valued such stock at $5 to $6 a share in 1968 as an investing principal and advisor to others. (Ex. 17, pp 4 & 5, Tr. 44-56)

30. Another expert witness for the petitioners was Herbert S. Cannon who at present is President and a Director of Philips, Appel & Walden, Inc., members of the New York Stock Exchange, Chairman of the

Board of Directors of Solvent Chemical Co., Inc. and Chairman of the Board of Directors of Cannon Industries, Inc. From 1962 to 1970 Mr. Cannon was President and a Director of Weis, Voisin & Cannon & Co., Inc. and predecessor firms (Members of the New York Stock Exchange). From 1967 to 1970, he was also Chairman of the Board of Directors of Elgin National Industries, Inc. (listed on New York Stock Exchange) and from 1970 to 1973 he was Chairman of the Board of Directors and President of Cannon, Jerold & Co., Inc. (members of the New York Stock Exchange. (Ex. 19, p. 1) Mr. Cannon holds and has held directorships in several publicly owned and listed corporations and has acted as financial consultant to numerous corporations including Bartell Media Corp., Elgin National Industries, The Franklin Mint, and Thompson-Starrett Corp. (Ex. 19, pp 1, 2)

31. Mr. Cannon has also been on the investment committee of the Tower Fund which invested approximately $6,000,000, and a Trustee of Washington and Jefferson College and a member of the finance committee which invests approximately $25,000,000. He has served as an appraiser in the sale and merger of several public and private corporations and qualified as an expert witness in seven arbitration and court proceedings requiring the evaluation of corporate worth. (Ex. 19, p. 3)

32. From 1962 to 1970 as President of Weis, Voisin, Cannon & Co., Inc., Mr. Cannon was totally responsible for all financial activities of the corporation to the extent of:

15 Private placements involving	$ 15,000,000
Underwritings, as Manager	100,000,000
Underwritings, as participant	200,000,000
Mergers and Acquisitions	15,000,000

(Ex. 19, p. 3)

33. Like Mr. Wit, Mr. Cannon's approach to the issue of valuation was from the market viewpoint based upon his own expertise and experience. The factors determining his valuation were: the lack of liquidity, lack of dividends and the inability to have a say in the management, planning, financial policies or in the possible sale or liquidation of Modern Maid Food Products, Inc. (Ex. 19, p. 6, Tr. 104,105)

34. Based on his experience Mr. Cannon believed a person taking a speculative position in non-voting, non-dividend paying stock in a closely held corporation requiring a substantial sum of money would anticipate a profit of at least 400% within a three-year period. Even if a public offering is effected, insider's stock is usually restricted for an additional period of years from public sale (Ex. 19, p.6, Tr. 105, 106)

35. Due to the relative flatness of earnings in 1965, 1966 and 1967, the maximum value that would be placed upon the company as a whole in August 1968 would be $6,158,000 or ten times average earnings in 1965 through 1967, if a public company, or $33.70 a common share after deducting preferred stock. (Ex. 19, p. 6) Allowing for a 400% profit that is required in speculative investments in non-marketable closely held situations, the most according to Mr. Cannon that would be paid for the Class B stock of Modern Maid Food Products, Inc., would be $6.75 a share. (Ex. 19, p. 6) Such a price would require an investment of $173,340 from each of two purchasers of 25,680 shares and $58,000 from each of three additional purchasers of 8,600 shares. It would be extremely difficult to find five speculative investors with such available funds willing to take the risk of being locked-in with non-voting stock in a privately owned company

with no return on investment. (Ex. 19, p. 6) If only one individual was available for such a purchase, an amount in excess of $500,000 would be required again diminishing the availability of buyers and reducing the market value to $5 a share (Ex. 19, p. 6, Tr. 107)

36. If a public offering or merger with a public entity could not be reasonably expected within a three year period of time, then Mr. Cannon would be loathe to invest or advise any one else to invest at more than the nominal amount of $2 a share (Ex. 19, p. 6, Tr. 106, 107, 111). This price would still require approximately $154,000. At $5 a share the investment would have to be in excess of $385,000, too significant an amount to work upon pure conjecture without a real possibility of liquidating one's investment. (Ex. 19, p. 6, Tr. 110,111)

37. The purchaser of Class B common stock without the ability to force management to change the status of the stock from non-voting common, could entertain no probability of ever liquidating the stock in the public market. Due to different class status none of the rules of the S.E.C. or N.A.S.D. (National Association of Security Dealers) permit an automatic registration, even after a substantial holding period to enable even piecemeal liquidation into the public market. (Ex. 19, p. 6,7, Tr. 107, 109) Such a factor alone would greatly depreciate the fair market value of the stock by 70% even where underwritings are being considered. (Ex. 19, p. 7)

38. A third expert witness for the petitioners was Gordon Smith of American Appraisal Co. That Company employs over 900 professional staff members and has served 300 of Fortunes tabulation of 500 largest

industrial corporations in the United States. Mr. Smith is a senior member of the American Society of Appraisers. (Ex. 18, p. 1)

39. Mr. Smith's approach to the valuation of the Class B common stock of Modern Maid Food Products, Inc. in August and September 1968 was a statistical one based upon a comparative analysis of prices of capital stock of publicly traded companies in as close as possible similar business, modified by limiting conditions under which the shares could be sold. (Ex. 18, p. 7, 8)

40. Mr. Smith concluded that the equity of Modern Maid Food Products, Inc. if offered on the public market would sell at a price/earnings ratio of 10. applied to average earnings of 1965, 1966 and 1967 of $616,000., or $6,160,000. (Ex. 8, p. 12, Tr. 85, 86) From this figure Mr. Smith deducted 15% for the costs of going public - underwriting fees, commissions, legal and consulting fees and management expense, giving a revised value of $5,236,000. (Ex. 18 p. 12, 13, Tr. 86) Mr. Cannon was also of the opinion that 15% was the minimum cost of going public for a company the size of Modern Maid Food Products, Inc. (Tr. 226-27)

41. The preferred stock of Modern Maid Food Products, Inc. was considered to have an equivalent rating to Standard & Poors BBB & BB preferred stocks and a market value of $80 a share or $2,016,000 for the 25,200 shares outstanding. (Ex. 18, pp. 13, 14, Tr. 87)

42. Mr. Smith valued the common equity of Modern Maid Food Products, Inc. at $29.81 a share for 108,000 common shares if all publicly traded with no restriction.
(Ex. 18, p. 15 Tr. 87)

43. During January 1 - July 24, 1968 the Value Line Development Capital Corporation purchased restricted shares of common stocks in twelve corporations that had similar securities publicly traded. The discounts on such purchases ranged from 16.7% to 71.4% and averaged 44%. More than one-half showed discounts of over 40% and their average discount was 57.2%. (Ex. 18, p. 16, Tr. 88)

44. At least 50% of the value of restricted securities in Value Line Development Capital Corporation portfolio were subject to a commitment from the issuer to register at Value Line's request the securities under the Security Act of 1933. (Ex. 18, p. 18) The 50% limitation on investment in private securities without a commitment for registration was to give the Value Line Development Capital Corp. as much latitude as possible. As a matter of fact 85%-90% of private stock purchases had commitments for registration. (Tr. 232,233)

45. Funds owning restricted shares of publicly traded company stock have access to financial data on the corporation and the value of the publicly traded shares serves as a benchmark to indicate the public investors appraisal of the company. Such information and guidepost were not available to a holder of only Class B common stock of Modern Maid Food Products, Inc. (Ex. 18, p. 19)

46. Mr. Smith was of the opinion that the Class B common stock had a fair market value of $11.50 a share in August and September 1968 based upon the 112,790 shares then outstanding. (Tr. 90)

47. Mr. Smith's valuation of $11.50 a share presupposes Modern Maid Food Products, Inc. becoming a publicly owned corporation. (Tr. 91) If there was no intention of going public, his valuation would

be substantially reduced. Mr. Smith deferred to those engaged in the marketing area in determining what the market would be as he had no experience in such a case. (Tr. 91, 92)

48. The respondent's expert, Hugh A. MacMullen, III, admitted he had no experience in counselling purchases of securities of closely held corporations. (Tr. 133)

49. Mr. MacMullen was not doing appraisal work in 1968. (Tr. 134)

50. Hugh MacMullen, respondent's expert, based his appraisal of the Class B common stock of Modern Maid Food Products, Inc. on five so-called "comparable" public companies. These were: Martha White Foods, Inc., B. Manischewitz Co., Bridgeford Foods Corp., Saps Foods, Inc., and Spaulding Bakeries, Inc. (Ex Q.) None of these companies were in any way a competitor of Modern Maid Food Products, Inc. (Tr. 33, 34, v. Ex. Q, pp. 37-43)

51. Martha White Foods, Inc. was a milling company that sold its end product in retail stores and processed and distributed corn meal, dried beans and mixed feed (for animals) as well as distributing convenience foods nationwide. Its annual volume in year ended June 1, 1968 was in excess of $40,000,000. (Ex. Q p. 37)

52. B. Manischewitz Co. makes matzos, matzo meal and farfel, cake meal, borscht (beet soup), gefilte fish, baby foods and canned soups. It distributes pickles, canned fruits, candies, kosher grocery items and sacramental wine. (Ex. Q p. 39) This company does not have a close relationship with Modern Maid Food Products, Inc. (Tr. 162). It was selected because Manischewitz matzos sold to retail stores has the same raw material ingredient as the products of Modern Maid Food Products, Inc. (Tr. 162)

53. Bridgeford Foods Corp. is engaged primarily in the manufacture and wholesale distribution of processed meats and other delicatessen foods, and sells fresh, frozen and smoked meats. (Ex Q. p. 41) Mr. MacMullen considered it comparable only because its third and least important field of activity, the manufacture and sale of frozen bread dough products, uses wheat flour. (Tr. 161, 162) Mr. MacMullen didn't know to what market, Bridgeford Foods sold its frozen dough products. (Tr. 162)

54. Saps Foods, Inc. is engaged primarily in the production and sale of bakery products to supermarkets, restaurants and vending machine operators; also operates three restaurants through subsidiaries. (Ex. Q. p. 42) This Company is related to Modern Maid Food Products, Inc. in that they are buying the same raw material. (Tr. 161)

55. Spaulding Bakeries, Inc. operates a bakery selling bread, rolls and crullers in New York, Connecticut and Pennsylvania. (Ex. Q. p. 43, Tr. 159) MacMullen didn't know to what market they sold. (Tr. 159)

56. Mr. MacMullen did not know what were the sales or income of alleged comparable companies from the activities that used the same raw material as that used by Modern Maid Food Products, Inc. - wheat flour. (Tr. 162, 163)

57. The so-called comparable companies used by respondent's expert are admittedly not comparable with Modern Maid Food Products, Inc. (Tr. 146, 150, Stip. 3, Tr. 11, 33, 34, Ex. Q pp. 37, 39, 41, 42, [illegible])

58. Mr. MacMullen acknowledged that if the last audit figures at the time of gift were for the year ended December 31, 1967, and no

interim figures were supplied by accountants for Modern Maid Food Products, Inc., an appraisal would have to be made on the basis of operations up to December 31, 1967. (Tr. 163)

59. A purchaser would look at as many prior years' earning figures as a company would have available (Tr. 164) A purchaser would be concerned to know if earnings of the three prior years were flat or showed growth and the market price would reflect whether there was a growth situation or not. (Tr. 164)

60. Mr. MacMullen's 8% cost for floating a public sale of stock is based upon figures of the Securities and Exchange Commission considerably before 1968 (Tr. 164). He did not know to what year they related. (Tr. 166)

61. The 8% cost used by Mr. MacMullen was just the underwriting cost. He admitted there were also costs for legal fees, accounting fees, and at times fees to underwriters in warrants and cheap stock (Tr. 166).

62. Mr. MacMullen couldn't name one company other than Modern Maid Food Products, Inc. that went public in 1968 or 1969 at a cost of 8%. (Tr. 166)

63. The market prices used by Mr. MacMullen on page 33 of Ex. Q in determining his appraisal value for Modern Maid Food Products, Inc. stock were the average of the high and low prices of the stocks in 1968 except for Bridgeford Foods. (Tr. 174)

64. Mr. MacMullen didn't know the average price at which Bridgeford Foods sold in 1968. He used the offering price of 100,000 shares in December 1968. Previously Bridgeford Foods had 600,000

shares outstanding before the new issue in December 1968. (Tr. 174).

65. Mr. MacMullen's average market price figures were obtained from Moody's (Annual Manuals). He did not know from where Moody's obtained its figures (Tr. 179). He just used them. He didn't know if they were correct. (Tr. 179)

66. The annual market price range in Moody's represents data obtained from the National Quotation Bureau (pink sheets). (Tr. 237, 238)

67. The dividends a company is paying is a factor in the price earnings ratio. (Tr. 180) The amount of dividends paid by Mr. MacMullen's "comparables" played no part in his determination of fair market value for the stock of Modern Maid Food Products, Inc. (Tr. 181, 182)

68. Saps Foods, Inc. earned 49¢, 71¢ and 90¢ a share in years ended May 31, 1967, 1968 and 1969, respectively, and paid no dividends. (Tr. 182)

69. Spaulding Bakeries had earnings of 81¢ and 77¢ a share in 1968 and 1969, respectively, and paid dividends of 52¢ a share in each year (Tr. 183).

70. Mr. MacMullen admitted that the fact that Spaulding Bakeries was paying a dividend may have been a factor why Spaulding Bakeries and Saps Foods had the same average market price in 1968 although Spauldings earnings were flat and Saps Foods showed marked growth of approximately 80% from year ended May 31, 1967 to May 31, 1969. (Tr. 183)

71. Market price of a stock takes into consideration all factors - sales, net worth, earnings, dividends, growth factor, sponsorship, floating supply and whatever other factors go into determining market price. (Tr. 185)

72. Mr. MacMullen didn't know whether the acquisition prices set forth on page 50 of Exhibit Q. were in cash or stock. (Tr. 205)

73. Even in the throes of 1968 when money was plentiful, purchasers were being generous in buying private stock without a right of registration at a discount of about 50%. (Tr. 231)

74. The most important factors in finding a purchaser for stock in a privately held corporation are the attractiveness of the venture and the ability to dispose of the stock subsequently. (Tr. 234, 235)

75. The business of Modern Maid Food Products, Inc. was not of the type that would attract venture capital. It was not the kind of growth industry venture capital was looking for in 1968. Its earnings were flat and venture growth capital was not interested in the food industry. (Tr. 235, 236)

76. A fairly conservative investor is concerned with his powers of control, the liquidity of his investment, the opportunity to revamp the asset holdings of the company, his net return by way of dividends as compared with other opportunities in the open market. (Tr. 155)

77. Investors are concerned about the length of time they might have to keep an investment, the degree of loss and risk compared to possible gain, possibility of liquidation of the investment, and the available market in which to dispose subsequently of stock. (Tr. 157)

78. The criteria used by an appraiser in selecting comparables are size, product, market, customers and trade name. (Tr. 158)

79. At the end of 1973, Modern Maid Food Products, Inc. had net worth of $9.08 a common share (App 1) and its common stock listed on the American Stock Exchange sold for $3 a share on July 10, 1974. (App 2) There were no sales after July 10, 1974 through July 29th, 1974.

80. Operations of Modern Maid Food Products, Inc. reflect a loss of $285,000(1) in the fourth quarter of 1973 and a loss of $263,000 in the first quarter of 1974 (App. 3 & 4)*

* with brief to Tax Court.

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(1) 9 months earnings to Sept. 30, 1973 - App. 3 $836,000
12 months earnings to Dec. 31, 1972 - App. 1 551,000
Loss in 4th quarter 1973 $285,000

T. C. Memo. 1974-285

UNITED STATES TAX COURT

SEYMOUR SILVERMAN, Et Al.,[1] Petitioners v. COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket Nos. 3707-72, 3708-72, 3709-72, 3710-72.

Filed November 6, 1974.

Sidney Gelfand and Wallace Musoff, for the petitioners.

Stanley J. Goldberg, for the respondent.

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[1] The cases of the following petitioners are consolidated herewith: Helen Silverman, docket No. 3708-72; Jack Silverman, docket No. 3709-72; and Frances Silverman, docket No. 3710-72.

MEMORANDUM FINDINGS OF FACT AND OPINION

QUEALY, Judge: The respondent determined deficiencies in gift tax to be due from petitioners for the calendar year 1968, as follows:

Docket No.	Petitioner	Deficiency
3707-72	Seymour Silverman	$116,902.50
3708-72	Helen Silverman	116,902.50
3709-72	Jack Silverman	259,087.20
3710-72	Frances Silverman	259,087.20
	Total	$751,979.40

The sole issue for decision relates to the determination of the value, within the meaning of section 2512,[2] of the shares of class B common stock of Modern Maid Food Products, Inc., on August 21, 1968 and September 24, 1968, the dates when petitioners made gifts of the stock to certain trusts.

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[2] All statutory references are to the Internal Revenue Code of 1954, as amended, unless otherwise indicated.

FINDINGS OF FACT

Some of the facts have been stipulated by the parties. Such facts and the exhibits attached thereto are incorporated herein by this reference.

Seymour Silverman and Helen Silverman are husband and wife. At the time of the filing of their petitions herein, they legally resided at Lynnbrook, New York. Seymour Silverman filed a U.S. Gift Tax return for the calendar year 1968 with the district director of internal revenue, Brooklyn, New York. Mrs. Helen Silverman consented to have the gifts made during the calendar year 1968 considered as having been made one-half by her and the other half by her spouse.

Jack Silverman and Frances Silverman are husband and wife. At the time of the filing of their petitions herein, they legally resided at Woodmere, New York. Jack Silverman filed a U.S. Gift Tax return for the calendar year 1968 with the district director of internal revenue, Brooklyn, New York.

Mrs. Frances C. Iverman consented to have the gifts made during the calendar year 1968 considered as having been made one-half by her and the other half by her spouse.

Modern Maid Food Products, Inc. (hereinafter referred to as "Modern Maid"), was organized on January 7, 1952, under the laws of the State of New York and has engaged in the business of manufacturing and selling breading and batter mixes for use by processors of shrimp, fish, and poultry, and the manufacturing and selling of prepared flour mixes for mass feeding outlets such as hospitals, restaurants, and hotels. The flour mixes are sold through wholesale grocers. Modern Maid is a successor to a partnership formed in 1933.

Modern Maid has two wholly-owned subsidiaries, Modern Maid Food Products of Louisiana, Inc., and Modern Maid Realty Corp., both incorporated under the laws of the State of Louisiana. The principal executive offices of Modern Maid were located at 110-60 Dunkirk Street, Jamaica, New York.

On April 22, 1968, the capitalization of Modern Maid, and the shares held by the respective shareholders, were as follows:

	Common Stock $100 Par Value	Preferred Stock $100 Par Value
Jack Silverman	1,284	265
Seymour Silverman	645	430
Harold Oppenheim	225	150
Stanley Silverman	3	10
Joel Silverman	3	10
Jack Silverman Foundation		575
Total	2,160	1,440

On April 22, 1968, Modern Maid Food Products, Inc., requested a ruling from the Commissioner of Internal Revenue that a proposed reorganization qualify as a tax-free reorganization under the provisions of section 368(a)(1)(E). Under the proposed reorganization, Modern Maid would increase authorized preferred stock $100 par value from 1,500 to 30,000 shares and create

two new classes of stock, namely (a) 24,000 shares of voting class A common stock par value $10 per share and (b) 96,000 shares of nonvoting class B common stock par value $10 per share. Each share of the original common stock would thereupon be exchanged for 10 shares new class A common par value $10 per share, 40 shares new class B common par value $10 per share, and 11 shares preferred par value $100 per share.

On June 28, 1968, the Commissioner of Internal Revenue issued his ruling with respect to Modern Maid's request of April 22, 1968.

On July 13, 1968, Modern Maid voted to adopt the proposed plan of reorganization, effective August 12, 1968. As a result of the reorganization,

the outstanding capital stock of Modern Maid Food Products, Inc., was held as follows:

	Class A Common $10 par value	Class B Common $10 par value	5% Common Preferred Stock $100 par value
Jack Silverman	12,840	51,360	14,389
Seymour Silverman	6,450	25,800	7,525
Harold Oppenheim	2,250	9,000	2,625
Stanley Silverman	30	120	43
Joel Silverman	30	120	43
Jack Silverman Foundation			575
	21,600	86,400	25,200

On August 12, 1968, Modern Maid entered into an agreement for the sale of unissued class B common stock to selected employees and legal counsel. The said agreement concerned purchases for investment purposes only and prohibited the subscribing stockholders from disposing of or encumbering their class B stock without the consent of the corporation. In absence of such consent or on the retirement or death of the subscribing stockholder, the agreement provided:

> * * * The party [the subscribing stockholder or his estate] * * * shall give to the Corporation written notice by certified mail of his intention, and such notice shall

> contain an offer to sell all his stock in accordance with the terms of this agreement, within thirty (30) days after the date of such notice, the stockholder giving such notice shall sell and the Corporation shall purchase all of such stockholder's stock.

The purchase price of each share was to be based on the value shown on the last Federal income tax return or on the annual financial statement, if such information was not on the return. The parties themselves could set any other value by agreement. Pursuant to this agreement, Modern Maid, in September 1968, sold 4,790 shares of its class B common stock to said employees and associates at $10 per share.

Gifts of class B common stock were made by Jack Silverman, Seymour Silverman and Harold Oppenheim on the dates and in the amounts set forth below:

Date	Donor	Donee	No. of Shares
8/21/68	Jack Silverman	Trust for Benefit of Joel Silverman	25,680
		Trust for Benefit of Stanley Silverman	25,680
		Total	51,360

Date	Donor	Donee	No. of Shares
9/24/68	Seymour Silverman	Trust for Benefit of Susan Silverman	8,600
		Trust for Benefit of Anne Silverman	8,600
		Trust for Benefit of Beth Silverman	8,600
		Total	25,800
12/8/68	Harold Oppenheim	Martin Oppenheim	2,000
		Sandra Oppenheim	2,000
		Trust for Benefit of Elysia Beth Oppenheim	2,000
		Trust for Benefit of Robert Alan Oppenheim	2,000
		Total	8,000

On December 31, 1968, the following positions were held by the persons listed below:

Name	
Jack Silverman	President and Director
Harold Oppenheim	Vice President and Director
Seymour Silverman	Secretary-Treasurer and Director
Stanley Silverman	Director

Jack Silverman, then 60 years of age, one of the founders of Modern Maid, had been its chief executive since 1957. Harold Oppenheim, then 54 years of age, had been employed by Modern Maid since 1954. Between 1954 and 1968, he served as superintendent in charge of plant operations and since 1968 had served as vice president in charge of plant operations. Seymour Silverman, then 49 years of age, had been employed by Modern Maid since 1952 and had served as secretary-treasurer since that time. Stanley Silverman, then 26 years of age, had been employed by Modern Maid continuously since 1967.

Beginning in March 1969, negotiations were initiated on behalf of Modern Maid with Ladenburg, Thalmann & Co., investment bankers, with a view towards the sale of stock of Modern Maid in a public offering.

A special meeting of the stockholders was called on June 16, 1969, to amend the certificate of incorporation of Modern Maid, and to take such other actions

as were necessary in order to meet the conditions prescribed in the agreement with Ladenburg, Thalmann & Co. for a public offering of the common stock of Modern Maid.

At this meeting of June 16, 1969, an amendment to the certificate of incorporation was adopted authorizing a capitalization consisting of 2 million shares of common stock of a par value of $1 per share with voting rights, and 100,000 shares of convertible preferred stock with such designations, relative rights, preferences and limitations, as might be set by the board of directors; a further amendment was adopted to provide that no shareholder shall have preemptive rights; and the permissible number of directors was increased to not less than three and not more than nine. A plan of reorganization was thereupon adopted whereby each share of then issued and outstanding preferred stock would be exchanged for 8.75 shares of the new common stock, each share of presently issued and outstanding class A voting stock would be exchanged for 7 shares of the new common stock, and

each share of the presently issued and outstanding class B voting stock would be exchanged for 6.5 shares of the new common stock.

At the same meeting, the proposal by Ladenburg, Thalmann & Co. for the underwriting and public sales of the shares of Modern Maid was approved and the appropriate authorizations to the offices and directors to proceed therewith were adopted.

Following the meeting of the stockholders on June 16, 1969, the exchange of the then outstanding class A common stock, class B common stock, and preferred stock was consummated in accordance with the plan adopted at the meeting.

On October 28, 1969, Ladenburg, Thalmann & Co. issued its prospectus whereby it made a firm commitment to underwrite and publicly sell 350,000 shares of the new common stock at $12 per share. It acquired 100,000 shares from the company and 250,000 from certain selling shareholders.

The Consolidated Balance Sheet of Modern Maid and its subsidiaries as of December 31, 1967, was as follows:

ASSETS		
CURRENT		
Cash	$ 497,715	
Accounts & Notes Receivable	2,656,444	
Inventories	415,458	
Certificate of Deposit	150,000	
Interest Receivable	4,029	$3,723,646
FIXED ASSETS		
Machinery & Equipment	1,636,987	
Furniture & Fixtures	87,927	
Leasehold Improvements	220,959	
Land & Building	343,358	
Truck Trailer	24,842	
	2,314,074	
Less: Reserve for Depreciation	1,039,470	1,274,604
OTHER ASSETS		
Deposits & Advances	54,027	
Investments	26,000	
Life Insurance - Cash Surrender Value	32,703	
Deferred Charges	13,415	
Net Leasehold	3,950	130,095
		$5,128,345
LIABILITIES & CAPITAL		
CURRENT		
Accounts Payable	744,138	
Taxes Withheld	25,036	
Accrued Expenses	237,496	
Federal Income Taxes	211,999	
Due to Officers	21,901	
Notes Payable	36,455	$1,277,025
NET WORTH		
Common Stock	216,000	
Preferred Stock	144,000	
Surplus	3,491,320	3,851,320
		$5,128,345

The Consolidated Statement of Operations of Modern Maid and subsidiaries for the period December 31, 1964 to 1968, inclusive, and the 6-month period ended June 30, 1968 and June 30, 1969, was as follows:[3]

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[3] The financial data for the taxable years ended December 31, 1964 and 1965 and for the 6-month period ended June 30, 1968, are unaudited.

	Year, December 31,					Six Months Ended June 30,	
	1964	1965	1966	1967	1968	1968	1969
Net Sales	$8,255,805	$9,771,555	$10,67[illegible]9	$11,739,411	$13,478,372	$6,290,394	$7,046,273
Cost of sales (Note B)	5,291,198	6,291,795	7,162,996	7,709,696	8,743,482	4,076,175	4,493,504
Gross Profit	2,964,607	3,479,760	3,510,773	4,029.715	4,734,890	2,214,219	2,552,769
Selling, general and administrative expenses (Notes A and B)	2,105,095	2,300,100	2,413,066	2,788,565	3,088,817	1,451,081	1,620,274
Income from operations	859,512	1,179,660	1,097,707	1,241,150	1,646,073	763,138	932,495
Other Income (deductions):							
Interest Income	11,977	23,382	39,247	44,854	56,928	33,610	30,536
Other, net	(15,378)	(7,958)	(9,583)	(1,610)	(124)	--	(1,971)
	(3,401)	15,424	29,664	43,244	56,804	33,610	28,565
Income before provision for income taxes	856,111	1,195,084	1,127,371	1,284,394	1,702,877	796,748	961,060
Provision for Income Taxes:							
Federal	393,483	522,567	479,362	558,575	817,750	374,713	477,558
State and City	36,881	50,035	58,786	90,158	96,878	41,949	52,807
	430,364	572,602	538,148	648,733	914,628	416,662	530,365
Net Income	$ 425,747	$ 622,482	$ 589,223	$ 635,661	$ 78[illegible],249	$ 380,086	$ 430,695

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After the 1968 recapitalization of Modern Maid, the earnings per share of the common stock based on the consolidated income for the taxable years 1964 to 1968, inclusive, were as follows:

	Shares Outstanding	1964	1965	1966	1967	1968
Net income		$425,747	$622,482	$589,223	$635,661	$788,249
Preferred Stock 5% cum. pref.	25,200	126,000	126,000	126,000	126,000	126,000
Class A common	21,600					
Class B common	91,190					
Earnings for common shares	112,790	299,747	496,482	463,223	509,661	662,249
Earnings per common shares		2.66	4.40	4.11	4.52	5.87

Modern Maid was engaged in the business of manufacturing and selling breading and batter mixes for use by processors of shrimp, fish and poultry, and the manufacturing and selling of prepared flour mixes for mass feeding outlets such as hospitals, restaurants and hotels. The flour mixes are sold through wholesale grocers.

Modern Maid Food Products, Inc. is a successor to a partnership formed in 1933. It had a long history of steady earnings and growth.

Modern Maid's three major competitors with regard to its breading and batter mix products were Newlywed Baking Co. of Chicago, DCA Food Industries (formerly Donut Corporation of America), and Griffith Laboratories of Toronto, Canada. Its chief competitors in the prepared flour mix field were Pillsbury Flour Mills, General Mills, and DCA Food Industries.

There were no public sales of the common stock of Modern Maid prior to the underwriting by Ladenburg, Thalmann & Co., referred to above. No evidence was presented to show any public or other sales of stock in any company which might be considered comparable to Modern Maid. A multiple of ten times average earnings was a reasonable basis for the valuation of the class A common stock of Modern Maid.

As of August 21, 1968, and as of September 24, 1968, the fair market value of the class A common stock of Modern Maid was not less than $40 per share. As of the same date, the fair market value of the class B common stock was not less than $25 per share.

OPINION

The sole issue presented in this case relates to the value for gift tax purposes of several gifts of class B common stock of Modern Maid, totaling 77,160 shares. The procedures for the valuation of such property are set forth in sections 25.2512-1 and 25.2512-2, Gift Tax Regs. Since there were no public sales of the stock in question, the parties have resorted to other factors in accordance with those regulations.

The petitioners had absolute control of Modern Maid. They proceeded to effect a plan of reorganization or recapitalization for the purpose of making a gift of an interest in the corporation to their children, at the same time affording an opportunity to selected employees and associates in the business to buy some stock in the corporation.

Pursuant to a plan of recapitalization effected August 12, 1968, the then outstanding 2,160 shares of common stock par value $100 per share were exchanged for 10 shares of class A common stock with a par value of $10 per share, 40 shares of class B common stock with a par value of $10 per share, and 11 shares of preferred stock with a par value of $100 per share. Simultaneously, by agreement dated August 12, 1968, Modern Maid issued 4,790 additional shares of class B common stock to selected employees and legal counsel for a price of $10 per share. Following these transactions, Modern Maid had outstanding 21,600 shares of class A common stock, 91,190 shares of class B common stock and 25,200 shares of preferred stock.

As a result of the recapitalization, Jack Silverman held 12,840 shares of class A common stock, 51,360 shares of class B common stock and 14,389 shares of preferred stock. On August 21, 1968, he made gifts in trust for the benefit of his children totaling 51,360 shares of class B common stock.

As a result of the recapitalization, Seymour Silverman held 6,450 shares of class A common stock, 25,800 shares of class B common stock, and 7,525 shares of preferred stock. On September 24, 1968,

he made gifts in trust for the benefit of his children totaling the 25,800 shares of class B common stock.

For gift tax purposes, the petitioners reported a valuation of $10 per share for the class B common stock. In his notice of deficiency, respondent determined that the stock had a value of $48 per share. In his brief, respondent contends for a value of $25 per share. In their brief, petitioners argue that the valuation of $10 per share was too high, claiming a value of not more than $5 per share.

In this proceeding, the Court is not called upon to consider the tax consequences of the reclassification of the class B nonvoting shares into voting shares and the public offering of such shares. Until such event took place, all that the donees received was a nonvoting interest in a family-controlled corporation. However, we cannot ignore the realities of the situation.

The occasion for the subsequent exchange of the nonvoting stock for voting stock, in order that an interest in the corporation could be sold to the

public, may not have been foreseen at the time of the recapitalization and gifts. This does not mean that a second step in the "giving process" was not contemplated at some future date, irrespective of that occasion.[4] If all petitioners had in mind was to make a gift of non-voting common stock to their children, the parties probably would not be before this Court. The fact that the offer of the shares to the employees and associates at $10 per share was coupled with the restrictions on the sale of such shares under certain conditions at book value further confirms that none of the transactions involved in this proceeding can be measured as one would an arm's length sale such as would be made to a stranger.

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[4] Petitioners offered proof that the transaction with Ladenburg, Thalmann & Co., which brought about the conversion of the class B nonvoting common stock, was not foreseen at the time of the gifts. This does not negate the respondent's claim that petitioner's future plans went beyond the first step, with which we are here concerned.

The basis upon which petitioners would value the class B common stock is concisely stated in a hypothetical question proposed in petitioners' reply brief as follows:

> * * * 'How much would I invest to acquire 25,680 shares of Class B nonvoting, nondividend paying stock of Modern Maid Food Products, Inc. in August 1968 knowing the earning history and book value up to December 31, 1967, knowing those controlling the business had no plan or intention of going public, knowing that the substantial salaries and preferred dividends vitiated any incentive to declare dividends on the common stock, and knowing that the management intended to leave control to their children?'

Nothing in this record would support the hypothesis that "those controlling the business had no plan or intention of going public," nor can we attribute to petitioners, who controlled the voting stock, an intent to refrain from declaring dividends, increasing their salaries at will, and otherwise acting to the detriment of the nonvoting stockholders. On the contrary, petitioners were in a quasi-fiduciary

relationship to the holders of the minority or non-voting interests.[5] As such, they would be required to act in good faith as far as the rights of the minority are concerned. Pepper v. Litton, 308 U.S. 295 (1939); Zahn v. Transamerica Corporation, 162 F. 2d 36 (C.A. 3, 1947). If that duty were breached, the minority shareholders could maintain a cause of action to prevent or redress any injuries. Doherty v. Mutual Warehouse Company, 245 F. 2d 609 (C.A. 5, 1957).[6] The only statement with which we are in agreement is that the intent of petitioners was to leave control of the corporation to their children. We are really being asked to look at the first step in the fulfillment of that intent.

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5 The only point on which the expert witnesses seemingly agreed was that the nonvoting stock should be treated the same as a minority interest in a closely-held corporation.

6 For a discussion with respect to the liability of the directors for failure to declare dividends, see Bittker and Eustice, Federal Income Taxation of Corporations and Shareholders, ¶8.02, p. 8-6 (3d Edition, 1971).

The expert testimony presented by petitioners with respect to the value of the class B common stock failed to take into account the fact that if petitioners intended to sell a substantial interest in Modern Maid--and the class B common stock represented approximately two-thirds of the equity after the preferred stock--they would have adopted a different course of action or there never would be a sale. Although Ladenburg, Thalmann & Co. was unquestionably the best qualified "expert" to express an opinion with respect to the value of the stock of Modern Maid, petitioners chose not to present the testimony of that firm.

An expert witness for respondent testified that the stock, giving consideration to its restricted character, had a fair market value as of the date of the gifts of $25 per share. His opinion is supported by a valuation for the common stock, as a whole, discounted for the lack of voting power and control. However, rather than look to opinion evidence with respect to the value of the class B common stock from

an "outsider," the Court would be inclined to give greater weight to the relative value of the class B common stock which the petitioners, who still had control of the corporation, attributed to that stock in the ensuing transaction whereby both classes of stock were exchanged for a single class of voting common stock.

At the time of the gifts, there were outstanding 21,600 shares of class A common stock and 86,400 shares of class B common stock. Contemporaneously therewith, an additional 4,790 shares of class B common stock were sold to selected employees and associates, making a total of 91,190 shares of class B common stock outstanding.

A few months later, petitioners approved the terms of a second reorganization whereby the class A common stock would receive 7 shares of a new common stock and the class B common stock would receive 6.5 shares of a new common stock, thereby attributing to the class B common stock a value equal to 65/70ths of the value of the class A common stock. As a result, the holders of 21,600 shares of class A common stock acquired 151,200

shares of the new common stock and the holders of 91,190 shares of class B common stock acquired 592,735 shares of the new common stock. In this proceeding, neither party has directly challenged the basis for the exchange. In fact, petitioners' main objection was that the value attributed to either class of stock, as of the date of the agreement with Ladenburg, Thalmann & Co., should not be taken as evidence of value on the dates of the gifts.

Irrespective of the value attributed to the new common stock by Ladenburg, Thalmann & Co. in connection with a public offering, the fact that the old class B common stock was given a parity of 6.5 to 7 with the old class A common stock provides a yardstick with which to measure the value of the former as of the dates of the gifts. At that time, the Court would find that the class A common stock had a fair market value of about $40 per share. Using the subsequent exchange as a basis, this would result in a fair market value of $37 per share for the class B common stock.

Accordingly, considering the record before us, the Court finds that the fair market value of the class B common stock of Modern Maid, as of August 21, 1968 and as of September 24, 1968, was not less than $25 per share.

Decisions will be entered under Rule 155.

UNITED STATES TAX COURT
FILED
NOV 26 1974

UNITED STATES TAX COURT

SEYMOUR SILVERMAN, ET AL.,	)	
Petitioners,	)	Docket Nos. 3707-72
v.	)	3708-72
		3709-72
COMMISSIONER OF INTERNAL REVENUE,	)	3710-72
Respondent.	)	

MOTION FOR ADDITIONAL FINDINGS OF FACT

Petitioners respectfully move pursuant to Rule 161 for further findings of fact deemed essential to a proper review of the opinion in the above entitled cases.

FOR CAUSE IT IS SHOWN that the following findings of fact requested by petitioners in their brief are supported by the record, to many of which respondent stated "no objection" or did not deny their accuracy.

Numbers 7, 8, 9, 12, 13, 14, 18, 20 through 23, 25 through 34, 35 prefaced with "Mr. Cannon testifed", 36, 37 prefaced with "Mr. Cannon testified," 38 through 56, 60 through 80.

Additional requested findings of fact supported by the record are:

U. S. TAX COURT
DENIED
NOV 26 1974
(Signed) William H. Quealy
JUDGE

The average return of net income on net worth at the beginning of the year for the comparable companies used by respondent's expert was 17.62%. (See computations on pages 28, 29 of petitioners' brief based on the data in Exhibit Q., pp. 27, 41, 42.)

The common stock equity of Modern Maid Food Products, Inc. at December 31, 1967 represented approximately 26% of the total assets. (Ex. 8-H) The alleged comparable companies used by the respondent's expert had an average common stock equity of 65% of total assets. (Computation on page 32 of petitioners' brief based on the data in Exhibit Q, pp. 38, 40, 41, 43)

All of the acquisitions cited in the government expert's appraisal report in the schedule on page 50, which was the basis for computing his discount of 25% for a minority interest, were for stock of the acquiring companies. (Prentice-Hall Capital Adjustment Service through 1969, pp. C-49, L-18, L-82, M-85, M-204, R-93, U-45)

WHEREFORE, it is prayed this motion be granted.

Respectfully submitted,

Sidney Gelfand

Wallace Musoff

Dated: November 21, 1974

Wallace Musoff
136 East 57th St.
New York, N.Y. 10022
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U. S. TAX COURT
FILED AT
1974

UNITED STATES TAX COURT

SEYMOUR SILVERMAN, ET AL., Petitioners,	:	Docket Nos. 3707-72, 3708-72, 3709-72, 3710-72
v.	:	
COMMISSIONER OF INTERNAL REVENUE, Respondent.	:	

MOTION FOR RECONSIDERATION OF OPINION

Petitioners respectfully move pursuant to Rule 161 for a reconsideration of the opinion in the above cases.

FOR CAUSE IT IS SHOWN that memorandum opinion 1974-285, filed by the Court on November 6, 1974 substantially erred and warrants reconsideration.

Petitioners respectfully submit that the Court erred as follows:

1. The Court adopted a method of valuation completely alien to any proposed by the respondent or petitioners. Such action deprived the petitioners of the right to offer rebuttal evidence or show in their brief the error in the use of such method.

The respondent made no attempt to either explain

or support the deficiency proposed in the statutory notice of deficiency. At the time of trial the respondent admitted error in his determination of $48 a share and submitted no evidence other than the appraisal report and testimony of Hugh MacMullen III to support a value of $25 a share. Petitioners and respondent exchanged their respective experts' appraisal reports prior to trial and petitioners prepared their case to show the invalidity of the respondent's expert's appraisal in concept, data selection and mathematical computations. Certainly the petitioners' due process rights are impaired when they are deprived of the right to refute a basis never advanced by the respondent, but used by the Court in its opinion. (1)

The Court in its opinion correctly states: (2)

> "The Court is not called upon to consider the tax consequences of the reclassification of the Class B nonvoting shares and the public offering of such shares. Until such

(1) That the method and data used were of the Court's own making is in part noted in the transcript on p. 206, line 15 through p.208, line 3.

(2) p. 20

> event took place, all that the donees received was a nonvoting interest in a family controlled corporation.

But then the Court proceeded to do what it stated it was not to do. In valuing the shares, it referred to the future public offering which even the Court itself recognized was brought about by a transaction occurring after the time of the gifts and not foreseen at the time of the gifts.(3)

The Court's advent into the realm of speculation about the donee's contemplation in Sept mber and October 1968 to "go public" at some future unspecified date, concerning which there isn't a scintilla of supportive evidence, was specifically banned by the Supreme Court in Olson v. U.S. 292 U.S. 246 (1934) when it stated (p.257)

> "Elements affecting value that depend upon events or combinations of occurrences which, while within the realms of possibility, are not clearly shown to be reasonably probable should be excluded from consideration, for that would be to allow mere speculation and conjecture to become a guide for the ascertainment of value -- a thing to be condemned in business transactions as well as in judicial ascertainment of truth." (emphasis added)

The Tax Court further stated:

> "The expert testimony presented by the petitioners failed to take into account the fact that if petitioners intended to sell

(3) p. 21

> a substantial interest in Modern Maid -- and the Class B stock represented approximately two-thirds of the equity after the preferred stock -- they would have adopted a different course of action or there never would have been a sale."(4)

Such "different course of action" for valuing the stock would convert the property into something other than what the petitioners were giving. To adopt a "different course of action", not set out by the Court, but presumably a public offering, would

(a) No longer be the property which was the actual subject of the gift, but some entirely different property, and

(b) Not be possible with non-voting stock.

To use publicly owned voting stock as the basis for valuation would be not only a horse of a different color, but an entirely different animal. It would represent loss of control by the donors of their company. This is something they were unwilling to do in any event -- even with respect to gifts to their own children.

2. The Tax Court erred in its rejection of the truly expert testimony of Herbert Cannon and Harold Wit with notable credits and long active experience in the advising

(4) p. 24

about and marketing of securities in the financial community. The testimony of such experts was not diminished upon cross examination or negated by contradictory evidence with respect to their special expertise. This testimony was rejected not because it wasn't valid, but only because the Court was of the opinion the donees would have marketed their stock in a different fashion or there wouldn't be any sale at all.

This argument of the unwillingness of a donor to sell at the price a willing buyer would pay was raised by the government in Whitmore v. Fitzpatrick 127 F. Supp. 710 (Conn. 1954), but rejected by that Court. In that case the Court found the fair market value of the underlying assets was $3,118 per share. Taxpayer's experts' testimony of obtainable market price ranged from $850 to $1200 per share for minority interests (a total of 73% had been given to three sons). The government argued the plaintiff, as the sole owner, would not be a willing seller at the only price which a buyer according to plaintiff's experts would buy. The Court (Judge Hincks) stated: "Surely this argument is irrelevant to the problem".

The District Court stressed the "extraordinary difficulty in finding a buyer who would invest something over $200,000 (200 shares at $1000 a share) in a minority

interest" in a company without an established dividend paying record. The District Court presumptively rejected the theory that a larger sum could be realized if a different method of marketing had been pursued by first converting the property into something else.

Imagine what difficulty would then exist to find two buyers who would pay more than $640,000 each (25,680 shares x $25) to buy minority interests of non-voting stock without a market in a company making prepared batter mixes and crumbs for breading! Jack Silverman's gifts were to 2 donees and Seymour Silverman's gifts were to 3 donees, not hundreds or thousands of donees, and the gifts should be valued accordingly.(5)

The Court failed to recognize that the different course of action to which it was referring would have involved a great many purchasers and would have been illegal at that time without a registration with the Securities and Exchange Commission. Such a registration and such marketing would have converted the property that was actually given to

(5) The Court itself expressed the opinion that Modern Maid Food Products, Inc. stock "wasn't the type of business that would attract so-called venture capital anyway;" (Tr. 235) and that parties with venture capital are not attracted to the type of business of Modern Maid Food Products, Inc. (Tr. 236). In both of these opinions the Court's opinion was confirmed by Herbert Cannon, an expert in raising venture capital. (Tr. 235, 236)

property of a different kind.[6] It is important to note that Section 25.2512-1 of the Commissioner's own regulations defines fair market value as "that price at which property would change hands between a willing buyer and a willing seller" - just one buyer not many buyers for each gift of stock in a closely held corporation. Rejecting the testimony of Herbert Cannon and Harold Wit, which was based on the nature of the property actually given, for the reason stated by the Court is, therefore, making a finding clearly contrary to the weight of the evidence.

3. Appraisal reports and testimony had been submitted by both respondent's and one of petitioners' experts using the price-earnings method of evaluation based on alleged comparable companies. Both experts applied this price-earnings ratio to total corportate net income from which was subtracted

(a) The estimated cost of the public offering.

(b) The value of the preferred stock.

(c) Discount(s) for minority interest and Class B stock infirmities.

The petitioners definitively demonstrated the inapplicability of the appraisal of respondent's expert[7] and the Court

(6) Just as gifts of closely held stock may not be aggregated for valuation (Whitemore v. Fitzpatrick, supra, William Rushton, et al. 60 TC 272, reviewed by the Court and affirmed 5th Cir. 7/26/74), they may not be broken up for valuation, particularly when such breakup would be a violation of the Securities and Exchange Act or a conversion into different property.

(7) Petitioners' Brief pp. 26-41

was of similar opinion at the time of trial.[8]

The Court in its findings of fact stated:

> "A multiple of ten times average earnings was a reasonable basis for valuation of the Class A Common stock of Modern Maid."

No basis for this finding was given or exists in the record. Petitioners' expert, Gordon Smith of the American Appraisal Company did use that multiple of earnings in his report, but that was a multiple of total corporate earnings based upon an assumed public offering and from which initial total value deductions were taken for the cost of going public, the value of the preferred stock and the discount applicable to minority interest and Class B stock infirmities. The Court has used the same ten times earnings multiple, but applied it to the pro-forma earnings per share of Modern Maid Food Products, Inc., as if Modern Maid Food Products, Inc. was already a public company, which it wasn't, and without making the deductions used by both Respondent's and Petitioners' experts. If these deductions were made, a quite different valuation would result.

The government's expert used an 8% factor for cost of going public. He admitted that was purely for underwriting.

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(8) Tr. p.190 - The Court "I think Mr. Gelfand that that's why the Court came back to the basic proposition that if you want to, ... there are so many factors missing that the Court would be inclined to entertain a motion that we strike all of them (the appraisals) frankly."

writing cost. He didn't know any company other than Modern Maid Food Products, Inc. that paid only 8% for an underwriting in 1968 or 1969 for a small offering. In addition, there are costs for legal fees, accounting fees and administrative costs. Mr. Smith, petitioners' expert, taking these other costs into consideration used a cost factor of 15% which percent was supported by the testimony of Herbert Cannon with vast experience in the underwriting field. It is pertinent to note that in Inga Bardahl TCM 1965-158, the respondent's own expert discounted the price-earnings determination of fair market value by 20% for the cost of going public.

The government's only expert witness in this case stated discounts for minority interests vary from 10% to 50% from otherwise fair market value. He used a 25% discount factor computed on his schedule on page 50 of his appraisal report. The non-applicability of his comparatives as well as the mathematicl errors have been commented upon at length in petitioners' original brief.

The cases cited by government's own expert in Exhibit Q relfect the following percentages of discount for minority interest.

Drybrough v. U.S.	35%
Obermer v. U.S.	33 1/3%

The actual purchases of twelve minority interests by the Value Line Development Corp. in January - July 1968 are set out in Exhibit 18 in a schedule entitled "Exhibit 3." This data was for restricted shares of publicly traded securities and thus enjoyed a somewhat more favorable position than a minority interest in a closely held corporation with no market for its shares.

The Discounts for minority interests in this chart vary from a low of 16.7% to a high of 71.4% with a mean of 44% and a median of 42%.

Toward the end of 1969 when Modern Maid Food Products, Inc. became publicly owned, a discount of 8% was recognized for the Class B Common stock from the Class A Common stock, although Mr. MacMullen determined a discount of 16 2/3% or a maximum of $5 a share.

Applying these facts to a ten times earnings valuation if public, gives the following result:

Average earnings of 4 years prior to the gifts	$	570,000
Value of Company (10 times earnings)		5,700,000
Less Cost of going public -15%		850,000
Balance	$	4,850,000
Preferred stock		2,520,000
Value to common stock	$	2,330,000
Value per share (÷ 112790)	$	20
Discount for minority interest 35%		7
	$	13
Discount for Class B Limitation-8%		1
Value Class B Common stock -	$	12

Using the government expert's return on net worth approach, which method eliminates the vagaries of the market place, and correcting for mathematicl and other errors in Mr. MacMullen's use of the data, gives the following result:

Comparables' average of net income as a percent of net worth at the beginning of the year was 17.62% (see petitioners' brief pp. 28, 29)

	1/1/68	6/30/68
Net Worth per books	3,850,000	4,200,000
Comparables' % of return	17.62%	17.62%
Relative Net Income	$ 678,000	$ 740,000
Earnings - 6 mos. $380,000 x 2	760,000	760,000
Excess Earnings	82,000	20,000
Capitalized at avg.rate of return	17.62%	17.62%
Goodwill	465,000	110,000
Net Worth per Books	3,850,000	4,200,000
Value of Company	4,315,000	4,310,000
Preferred stock	2,52 ,000	2,520,000
Balance of Common Stock	1,795,000	1,790,000
Computed value of common stock	$ 1,800,000	
÷ 112,790 shares		$16 a share
Discount for minority interest and no market-35%		5.60 "
		10.40
Discount for Class B limitations-8%		.80
Value Class B Common stock		$ 9.60

4. The Court also erred in its application of the burden of proof rule. Once the Commissioner acknowledged that his original $48 a share value determination was in error, his presumption of correctness disappeared as the Court noted.(9)

When the determination of the Commissioner is found to be invalid, the determination made by the Tax Court "must be based upon substantial evidence and it is incumbent upon the Commissioner, not the taxpayer, to come forward with that evidence."(10) (emphasis added)

To the same effect is the decision in Helvering v. Taylor 70 F. 2d 619 (2nd Cir. 1934) affirmed 293 U.S. 507 (1935). In the Taylor case the Court of Appeals for the Second Circuit said:

> "If the burden of proof goes so far as to demand not only that the taxpayer show that the deficiency assessed against him is wrong, but what is the proper deficiency, or that there should be none at all, the decision (B.T.A.) was right even though we know the tax is too high. In an action to recover taxes unlawfully collected the burden does go so far. (citations) But the reason for this is obvious; a plaintiff, seeking an affirmative judgment measured in dollars, must prove how much is due. His claim is for money paid and he must show that every dollar he recovers is unjustly withheld. So it is not enough merely to prove

(9) Tr. 207.

(10) Kaufman v. Commissioner 18 AFTR 2d 6031 (4th Cir. 1966). This rule may not apply in the case of deductions.

> that the tax as a whole was unlawful; some of the dollars he paid may nevertheless have been due. But this reasoning does not apply when the proceeding is to review an assessment. Although that does indeed partake of the nature of a judgment, and the taxpayer has the burden of proving that it was wrong, after he has done so, he need not, at least under ordinary principles of procedure, prove that he owed no tax, or what was the tax that he did owe. The original assessment rested upon a finding, presumptively correct, but the presumption of its correctness does not extend to other findings which the Commissioner has never made. Any other result would invert the ordinary rules of procedure by imposing a burden of establishing a negative upon the obligor; indeed of disproving the existence of all possible obligations. (emphasis supplied)

In Federal National Bank of Shawnee, Oklahoma v. Commissioner 180 F. 2d 494 (10th Cir. 1950) the Court stated:

> "The burden of proof was on the taxpayer to show that the Commissioner's determination was invalid, but to meet that burden it was sufficient for the taxpayer to show that the determination was excessive and invalid. The taxpayer was not required to prove that he owed no tax or the correct amount of tax he did owe. It may not be held that he is bound to pay a tax that confessedly he does not owe, unless his evidence was sufficient also to establish the correct amount of tax, if any, that might be lawfully exacted." (emphasis added)

See also A & A Tool & Supply Co. et al. v. Commissioner 182 F. 2d 300 (10th Cir. 1950)

In the instant case the Commissioner's determination in the statutory notice was admittedly in error when he opted for $25 a share instead of the original $48 a share.

Despite the burden of proof now being on the Commissioner, the Tax Court holds petitioners' proof that "going public" was not foreseen at the time of gift "does not negate the respondent's claim that petitioner's future plans went beyond the first step, with which we are here concerned."(11)

The Court also stated "Although Ladenberg, Thalmann & Co. was unquestionably the best qualified 'expert' to express an opinion with respect to value of the stock of Modern Maid, petitioners chose not to present the testimony of the firm."(12)

Petitioners submit the burden of proof being upon the Commissioner, once he acknowledged error in his original determination, it was not incumbent upon them to disprove a mere "claim" of the respondent with respect to petitioners' future plans, or to call Ladenberg, Thalmann & Co.

(11) T.C. Opinion, p. 21, fn. 4

(12) p. 24

even assuming they were the best qualified experts to value the kind of stock given as a gift in 1968.

With respect to future plans of "going public", the record does contain the following.(13)

Q. "Up to and including the time of the gifts, did you have any intention for Modern Maid Food Products, Inc. to become a publicly owned corporation or to merge or sell said corporation? (emphasis added)

A. (Jack Silverman) No, there was not."(14)

There is no basis in the record nor has respondent or the Court even intimated any challenge to the credibility of Jack Silverman. In fact the only evidence in the record on this point (exhibits and testimony) shows that going public was a happenstance arising out of events occurring after the gifts were made. The respondent submitted no proof that the petitioners at the time of the gifts contemplated going public at some future unspecified date.

The Courts alluding to petitioner's responsibility and failure to call Ladenberg Thalmann & Co. is unwarranted since respondent had the burden of proof.(15)

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(13) Tr. 13

(14) p. 21 fn 4

(15) Respondent's efforts to contact a knowledgeable party from Ladenberg, Thalmann & Co. were fruitless since such party was no longer available, being somewhere in Texas.

5. In its reply brief petitioners posed a question containing the statement "knowing that the substantial salaries and preferred dividends vitiated any incentive to declare dividends on the common stock".

The Court has interpreted those words to imply "an intent to refrain from declaring dividends, increasing their salaries at will and otherwise acting to the detriment of non-voting shareholders" and proceeds to demolish that straw man. The fact is that the receipt of substantial salaries and preferred dividends does weaken the incentive to declare common stock dividends; such failure to declare dividends need not be violative of a quasi-fiduciary relationship. Any knowledgeable buyer of such shares would be aware of such condition which would obviously affect the price he would be willing to pay. Who wants to buy into a company for the purpose of charging and proving violations of a quasi-fiduciary relationship? As a matter of fact the record shows no dividends have been declared on the common stock of Modern Maid Food Products, Inc. after December 31, 1967 to the time of trial in 1974.

6. Petitioners recognize that values in any particular case are factual and specific to the particular case, but the opinion and determination of the Court has

no precedent in any guidelines heretofore set out by other courts, upon which guidelines, taxpayers and their counsel have a right to reply.

In Righter v. United States (Ct.Cl. 1961) 439 F. 2d 1204, there is the following comment:

> "The Comparative Appraisal method produces, nevertheless,no magic formula which rigidly gives the exact valuation answer. Companies are rarely identical in size, operation, or product and allowances must be made as the statute says, for 'all other factors'. This would necessarily include the very fact of unmarketability of the stock of a closely held corporation. In the last analysis much necessarily depends on the informed judgment of the knowledgeable investor concerning the refinements and adjustments to be made in arriving at the ultimate valuation figure. Thus it is not surprising that in this field the opinions of experts are considered to be peculiarly appropriate. (emphasis supplied)

In Whitemore v. Fitzpatrick (Conn. 1954) 121 F. Supp. 710, Judge Hincks agreed that power of control, liquidity of the investment, opportunities to revamp business and asset holdings, net return by way of dividends as compared with other opportunites in the open market, the tax aspects of the purchase are the factors a level-headed investor contemplating a large investment would make. The Court stated:

> "In view of the lack of market for the stock, there would be extraordinary difficulty in finding a buyer who would invest something over $200,000 in a minority interest in a Naugatuck corporation such as the Whitemore Company without an established

> dividend record of which about one-quarter in value of assets was in non-liquid form."

It should be noted the Court found the actual value to be $3118 per share, but the fair market value to be only $1057 per share, a discount of 66% for three closely held minority interests which formed a 73% majority in the aggregate.

In Estate of Gregg Maxcy T.C. Memo 1969-158 the Court stated:

> "In the instant case we are attempting to determine a price a willing seller of Maxcy Securities shares could get from a willing buyer, not what a buyer may eventually realize." (emphasis supplied)

In Richard Makeoff T.C. Memo 1967-13, 99% of the total common stock capitalization represented by non-voting stock was ascribed a value of 60% of the total capitalization -- in effect a discount of almost 40% solely due to its being non-voting stock.

In Morris Messing 48 T.C. 502, (1967) stock was sold to an underwriter on June 15, 1961 at a price equal to $9.80 a new share. The stock was split on June 30, 1961 preparatory to going public, gifts were made on September 13th and 16th, 1961 and a registration statement filed with the S.E.C. on September 27th, 1961. The respondent in

valuing the stock used as a starting point the market value when the company became publicly owned, less than 4 months after the date of the gifts.

The Court in that case rejected this approach stating "a publicly traded stock and a privately traded stock are not as respondent would have us assume, the same animal distinguished only by size, frequency or color of its spots. The essential nature of the beast is different." The Court further stated:

> "It is a matter of common knowledge that, as a result of the vagaries of the stock market and other national and international events, many a contemplated public offering never sees the light of day, and that because of factors effecting the market at the particular moment of the public offering, the offering price can be radically different from the one originally contemplated. In September 1961, there was no probable basis for predicting a public offering would in fact take place and even less for estimating the particular price of the offering."

If this is true in a case where a preliminary registration is made during the month of the gift, how remote and speculative are the possibilities where a public issue is never even contemplated at the time of the gifts, events happen that lead to negotiations beginning 7 months later, and the public offering is 14 months later?

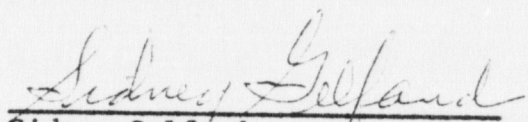
See also Bruce Berckmanns T.C. Memo 1961-100 and the principles enunciated therein.

Petitioners feel particularly aggrieved with the opinion of the Court since at the Court's urging effective settlement negotiations had been undertaken by the parties' counsel with respect to both 1968 and 1969 claimed gift tax deficiencies. Counsel had tentatively agreed on a basis of settlement of stock value of $10 a share for 1968, which would result in no deficiencies for that year, and an additional constructive gift of $4 a share in 1969 as a result of the reorganization. Settlement for 1969 was subject to agreement by the appellate division of the Internal Revenue Service since the trial of the deficiencies for 1969 had not yet been calendared. The settlement values were in accord with principles contained in advice from the national office of the Internal Revenue Service.

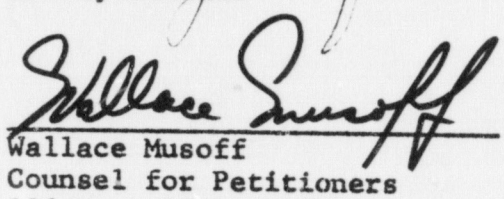
Report to the Court of settlement progress was awaiting a call from the Court, when the Court's opinion was received setting a value of $25 a share.

WHEREFORE it is prayed that this motion be granted.

Respectfully submitted,



Sidney Gelfand



Wallace Musoff
Counsel for Petitioners
136 East 57th Street
New York, N.Y. 10022

(212) 753-2900

Dated: November 25, 1974.

UNITED STATES TAX COURT

SEYMOUR SILVERMAN, Petitioner,	)	
v.	)	Docket No. 3707-72
COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $43,890.00.

(signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

By: /s/
GERALD BACKER,
Act'g Asst. Regional Counsel,
26 Federal Plaza (12th Fl.),
New York, New York 10007,
Tel. No. 212-264-8134.

/s/ Sidney Gelfand
SIDNEY GELFAND,
Counsel for Petitioner,
136 East 57th Street,
New York, New York 10022,
Tel. No. 212-753-2900.

UNITED STATES TAX COURT

HELEN SILVERMAN,	)	
	)	
Petitioner,	)	
	)	
v.	)	Docket No. 3708-72
	)	
COMMISSIONER OF INTERNAL REVENUE,	)	
	)	
Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $43,890.00.

(Signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

By: /s/
GERALD BACKER,
Act'g Asst. Regional Counsel,
26 Federal Plaza (12th Fl.),
New York, New York 10007,
Tel. No. 212-264-8134.

Sidney Gelfand
SIDNEY GELFAND,
Counsel for Petitioner,
136 East 57th Street,
New York, New York 10022,
Tel. No. 212-753-2900.

UNITED STATES TAX COURT

JACK SILVERMAN,	)	
	)	
Petitioner,	)	
	)	
v.	)	Docket No. 3709-72
	)	
COMMISSIONER OF INTERNAL REVENUE,	)	
	)	
Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $94,395.00.

(Signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

By: _____
GERALD BACKER,
Act'g Asst. Regional Counsel,
26 Federal Plaza (12th Fl.),
New York, New York 10007,
Tel. No. 212-264-8134.

/s/ Sidney Gelfand
SIDNEY GELFAND,
Counsel for Petitioner,
136 East 57th Street,
New York, New York 10022,
Tel. No. 212-753-2900.

UNITED STATES TAX COURT

FRANCES SILVERMAN, Petitioner,	)	
v.	)	Docket No. 3710-72
COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $94,395.00.

(signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

By: _____
GERALD BACKER,
Act'g Asst. Regional Counsel,
26 Federal Plaza (12th Fl.),
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/s/ Sidney Gelfand
SIDNEY GELFAND,
Counsel for Petitioner,
136 East 57th Street,
New York, New York 10022,
Tel. No. 212-753-2900.

STATUTE, LAW AND REGULATIONS

CONSTITUTION OF THE UNITED STATES

V AMENDMENT

"No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any Criminal Case to be a witness against himself, nor be deprived of life, liberty or property, without due process of law; nor shall private property be taken for public use, without just compensation." (Emphasis Supplied)

STATUTES

UNITED STATES Code, TITLE 15
Sec. 77d. Exempted transactions

The provisions of section 77e of this title shall not apply to--

(1) transactions by any person other than an issuer, underwriter, or dealer.

(2) transactions by an issuer not involving any public offering.

(3) transactions by a dealer (including an underwriter no longer acting as an underwriter in respect of the security involved in such transaction), except--

(A) transactions taking place prior to the expiration of forty days after the

first date upon which the security was bona fide offered to the public by the issuer or by or through an underwriter,

* * * *

Sec. 77e. Prohibitions relating to interestate commerce and the mails

*a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly--

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly--

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security with respect to which a registration statement has been filed under this sub-chapter, unless such prospectus meets the requirements of section 77j of this title; or

(2) to carry or cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of subsection (a) of section 77j of this title.

(c) It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the

use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 77h of this title.

UNITED STATES CODE, TITLE 26.

Sec. 2512 - VALUATION OF GIFTS

(a) If the gift is made in property, the fair market value thereof at the date of gift shall be considered the amount of the gift.

REGULATIONS UNDER INTERNAL REVENUE CODE

Sec. 25.2512-1. Valuation of property; in general

Section 2512 provides that if a gift is made in property, its value at the date of the gift shall be considered the amount of the gift. The value of the property is the price at which such property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell, and both having reasonable knowledge of relevant facts. The value of a particular kind of property is not the price that a forced sale of the property would produce....

Sec. 25.2512-2. Stocks and bonds--(a) In general. The value of stocks and bonds is the fair market value per share or bond on the date of the gift.

(b) Based on selling prices. (1) In general, if there is a market for stocks or bonds, on a stock exchange, in an over-the-counter market or otherwise, the mean between the highest and lowest quoted selling prices on the date of the gift is the fair market value per share or bond. If there were no sales on the date of the gift but there

were sales on dates within a reasonable period both before and after the date of the gift, the fair market value is determined by taking a weighted average of the means between the highest and lowest sales on the nearest date before and the nearest date after the date of the gift. The average is to be weighted inversely by the respective numbers of trading days between the selling dates and the date of the gift....

MISCELLANEOUS

Please note that Section 4(1) of the Securities Act of 1933 has been renumbered as Section 4(2)

For RELEASE Tuesday, November 6, 1962

SECURITIES AND EXCHANGE COMMISSION
Washington 25, D. C.

SECURITIES ACT OF 1933
Release No. 4552

NON-PUBLIC OFFERING EXEMPTION

The Commission today announced the issuance of a statement regarding the availability of the exemption from the registration requirements of Section 5 of the Securities Act of 1933 afforded by the second clause of Section 4(1) of the Act for "transactions by an issuer not involving any public offering," the so-called "private offering exemption." Traditionally, the second clause of Section 4(1) has been regarded as providing an exemption from registration for bank loans, private placements of securities with institutions, and the promotion of a business venture by a few closely related persons. However, an increasing tendency to rely upon the exemption for offerings of speculative issues to unrelated and uninformed persons prompts this statement to point out the limitations on its availability.

Whether a transaction is one not involving any public offering is essentially a question of fact and necessitates a consideration of all surrounding circumstances, including such factors as the relationship between the offerees and the issuer, the nature, scope, size, type and manner of the offering.

The Supreme Court in S.E.C. v. Ralston Purina Co., 346 U.S. 119, 124, 125 (1953), noted that the exemption must be interpreted in the light of the statutory purpose to "protect investors by promoting full disclosure of information thought necessary to inform investment decisions" and held that "the applicability of Section 4(1) should turn on whether the particular class of persons affected need the protection of the Act." The Court stated that the number of offerees is not conclusive as to the availability of the exemption, since the statute seems to apply to an offering "whether to few or many." 1/ However, the Court indicated that "nothing prevents the Commission, in enforcing the statute, from using some kind of numerical test in deciding when to investigate particular exemption claims." It should be emphasized, therefore, that the number of persons to whom the offering is extended in relevant only to the question whether they have the requisite association with and knowledge of the issuer which make the exemption available.

Consideration must be given not only to the identity of the actual

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1/ See, also, Gilligan, Will & Co. v. S.E.C., 267 F. 2d 461, 467 (C.A. 2, 1959), cert. denied, 361 U.S. 896 (1960).

purchasers but also to the offerees. Negotiations or conversations with or general solicitations of an unrestricted and unrelated group of prospective purchasers for the purpose of ascertaining who would be willing to accept an offer of securities is inconsistent with a claim that the transaction does not involve a public offering even though ultimately there may only be a few knowledgeable purchasers. 2/

A question frequently arises in the context of an offering to an issuer's employees. Limitation of an offering to certain employees designated as key employees may not be a sufficient showing to qualify for the exemption. As the Supreme Court stated in the Ralston Purina case: "The exemption as we construe it, does not deprive corporate employees, as a class, of the safeguards of the Act. We agree that some employee offerings may come within Section 4(1), e.g., one made to executive personnel who because of their position have access to the same kind of information that the Act would make available in the form of a registration statement. Absent such a showing of special circumstances, employees are just as much members of the investing 'public' as any of their neighbors in the community." The Court's concept is that the exemption is necessarily narrow. The exemption does not become available simply because offerees are voluntarily furnished information about the issuer. Such a construction would give each issuer the choice of registering or making its own voluntary disclosures without regard to the standards and sanctions of the Act.

The sale of stock to promoters who take the initiative in founding or organizing the business would come within the exemption. On the other hand, the transaction tends to become public when the promoters begin to bring in a diverse group of uninformed friends, neighbors and associates.

The size of the offering may also raise questions as to the probability that the offering will be completed within the strict confines of the exemption. An offering of millions of dollars to non-institutional and non-affiliated investors or one divided, or convertible, into many units would suggest that a public offering may be involved.

When the services of an investment banker, or other facility through

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2/ Reference is made to the so-called "investment clubs" which have been organized under claim of an exemption from the registration provisions of the Securities Act of 1933 as well as the Investment Company Act of 1940. It should not be assumed that so long as the investment club, which is an investment company within the meaning of the latter Act, does not obtain more than 100 members, a public offering of its securities, namely the memberships, will not be involved. An investment company may be exempt from the provisions of the Investment Company Act if its securities are owned by not more than 100 persons and it is not making and does not presently propose to make a public offering of its securities. (Section 3(c)(1)). Both elements must be considered in determining whether the exemption is available.

which public distributions are normally effected, are used to place the securities, special care must be taken to avoid a public offering. If the investment banker places the securities with discretionary accounts and other customers without regard to the ability of such customers to meet the tests implicit in the Ralston Purina case, the exemption may be lost. Public advertising of the offerings would, of course, be incompatible with a claim of a private offering. Similarly, the use of the facilities of a securities exchange to place the securities necessarily involves an offering to the public.

An important factor to be considered is whether the securities offered have come to rest in the hands of the initial informed group or whether the purchasers are merely conduits for a wider distribution. Persons who act in this capacity, whether or not engaged in the securities business, are deemed to be "underwriters" within the meaning of Section 2(11) of the Act. If the purchasers do in fact acquire the securities with a view to public distribution, the seller assumes the risk of possible violation of the registration requirements of the Act and consequent civil liabilities. 3/ This has led to the practice whereby the issuer secures from the initial purchasers representations that they have acquired the securities for investment. Sometimes a legend to this effect is placed on the stock certificates and stop-transfer instructions issued to the transfer agent. However, a statement by the initial purchaser, at the time of his acquisition, that the securities are taken for investment and not for distribution is necessarily self-serving and not conclusive as to his actual intent. Mere acceptance at face value of such assurances will not provide a basis for reliance on the exemption when inquiry would suggest to a reasonable person that these assurances are formal rather than real. The additional precautions of placing a legend on the security and issuing stop-transfer orders have proved in many cases to be an effective means of preventing illegal distributions. Nevertheless, these are only precautions and are not to be regarded as a basis for exemption from registration. The nature of the purchaser's past investment and trading practices or the character and scope of his business may be inconsistent with the purchase of large blocks of securities for investment. In particular, purchases by persons engaged in the business of buying and selling securities require careful scrutiny for the purpose of determining whether such person may be acting as an underwriter for the issuer.

The view is occasionally expressed that, solely by reason of continued holding of a security for the six-month capital-gain period specified in the income-tax laws, or for a year from the date of purchase, the security may be sold without registration. There is no statutory basis for such assumption. Of course, the longer the period of retention, the more persuasive would be the argument that the resale is not at variance with an original investment intent, but the length of time between acquisition and

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3/ See Release No. 33-4445.

resale is merely one evidentiary fact to be considered. The weight to be accorded this evidentiary fact must, of necessity, vary with the circumstances of each case. Further, a limitation upon resale for a stated period of time or under certain circumstances would tend to raise a question as to original intent even though such limitation might otherwise recommend itself as a policing device. There is no legal justification for the assumption that holding a security in an "investment account" rather than a "trading account," holding for a deferred sale, for a market rise, for sale if the market does not rise, or for a statutory escrow period, without more, establishes a valid basis for an exemption from registration under the Securities Act. 4/

An unforeseen change of circumstances since the date of purchase may be a basis for an opinion that the proposed resale is not inconsistent with an investment representation. However, such claim must be considered in the light of all of the relevant facts. Thus, an advance or decline in market price or a change in the issuer's operating results are normal investment risks and do not usually provide an acceptable basis for such claim of changed circumstances. Possible inability of the purchaser to pay off loans incurred in connection with the purchase of the stock would ordinarily not be deemed an unforeseeable change of circumstances. Further, in the case of securities pledged for a loan, the pledgee should not assume that he is free to distribute without registration. The Congressional mandate of disclosure to investors is not to be avoided to permit a public distribution of unregistered securities because the pledgee took the securities from a purchaser, subsequently delinquent. 5/

The view is sometimes expressed that investment companies and other institutional investors are not subject to any restrictions regarding disposition of securities stated to be taken for investment and that any securities so acquired may be sold by them whenever the investment decision to sell is made, no matter how brief the holding period. Institutional investors are, however, subject to the same restrictions on sale of securities acquired from an issuer or a person in a control relationship with an issuer insofar as compliance with the registration requirements of the Securities Act is concerned.

Integration of Offerings

A determination whether an offering is public or private would also include a consideration of the question whether it should be regarded as a part of a larger offering made or to be made. The following factors are relevant to such question of integration: whether (1) the different offerings are part of a single plan of financing, (2) the offerings involve

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4/ See Release No. 33-3825 re The Crowell-Collier Publishing Company.

5/ S.E.C. v. Guild Films Company, Inc. et al., 279 F. 2d 485 (C.A. 2, 1960), cert. denied sub nom., Santa Monica Bank v. S.E.C., 364 U.S. 819 (1960).

issuance of the same class of security, (3) the offerings are made at or about the same time, (4) the same type of consideration is to be received, (5) the offerings are made for the same general purpose.

What may appear to be a separate offering to a properly limited group will not be so considered if it is one of a related series of offerings. A person may not separate parts of a series of related transactions, the sum total of which is really one offering, and claim that a particular part is a non-public transaction. Thus, in the case of offerings of fractional undivided interests in separate oil or gas properties where the promoters must constantly find new participants for each new venture, it would appear to be appropriate to consider the entire series of offerings to determine the scope of this solicitation.

As has been emphasized in other releases discussing exemptions from the registration and prospectus requirements of the Securities Act, the terms of an exemption are to be strictly construed against the claimant who also has the burden of proving its availability. 6/ Moreover, persons receiving advice from the staff of the Commission that no action will be recommended if they proceed without registration in reliance upon the exemption should do so only with full realization that the tests so applied may not be proof against claims by purchasers of the security that registration should have been effected. Finally, Sections 12(2) and 17 of the Act, which provide civil liabilities and criminal sanctions for fraud in the sale of a security, are applicable to the transactions notwithstanding the availability of an exemption from registration.

6/ S.E.C. v. Sunbeam Gold Mining Co., 95 F. 2d 699, 701 (C.A. 9, 1938); Gilligan, Will & Co. v. S.E.C., 267 F. 2d 461, 466 (C.A. 2, 1959); S.E.C. v. Ralston Purina Co., 346 U.S. 119, 126 (1953); S.E.C. v. Culpepper et al, 270 F. 2d 241, 246 (C.A. 2, 1959).

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

SECURITIES ACT OF 1933
Rel. No. 5487 /April 23, 1974

NOTICE OF ADOPTION OF RULE 146 UNDER THE SECURITIES ACT OF 1933--
"TRANSACTIONS BY AN ISSUER DEEMED NOT TO INVOLVE ANY PUBLIC OFFERING"

(EFFECTIVE DATE: JUNE 10, 1974)

The Securities and Exchange Commission today announced the adoption of Rule 146 under the Securities Act of 1933 ("Act") which had been first noticed for comment in Securities Act Release No. 5336 (November 28, 1972) and which had been reproposed for comment in revised form in Securities Act Release No. 5430 (October 10, 1973). The adopted rule reflects a number of changes from the rule as last proposed. The changes are discussed in this release.

The Rule is designed to provide more objective standards for determining when offers or sales of securities by an issuer would be deemed to be transactions not involving any public offering within the meaning of Section 4(2) of the Act and thus would be exempt from the registration provisions of the Act. The Rule is available only to issuers since Section 4(2) provides an exemption for only the issuer. The Rule is not, however, the exclusive basis for determining whether that exemption is available. Accordingly, although persons claiming the exemption have the burden of proving its availability, persons may continue to rely on the Section 4(2) exemption by complying with the relevant administrative and judicial interpretations in effect at the time of the transaction. The protection afforded by the Rule, however, is available only to those who satisfy all its conditions.

* * * *

RULE 146

This release contains a general discussion of the background, purpose and general effect of the Rule to assist in a better understanding of its provisions. A brief analysis of each paragraph of the Rule is also included. However, attention is directed to the Rule itself for a more complete understanding.

BACKGROUND AND PURPOSE

Congress, in enacting the federal securities laws, created a continuous disclosure system designed to protect investors and to assure the

maintenance of fair and honest securities markets. The Commission, in administering and implementing these laws, has sought to coordinate and integrate this disclosure system with the exemptive provisions provided by such laws. Rule 146 is a further effort in this direction.

The legislative history of the Securities Act of 1933 indicates that the main concern of Congress was to provide full and fair disclosure in connection with the offer and sale of securities. However, Congress recognized that there were certain situations in which the protections afforded by the Act were not necessary. Concerning those specified exemptions from the Act, of which Section 4(2) is one, the House Report stated that "The Act carefully exempts from its application certain types of . . . securities transactions where there is no practical need for its application or where the public benefits are too remote."1/

Section 4(2) of the Act provides that "the provisions of Section 5 shall not apply to . . . transactions by an issuer not involving any public offering." The phrase "transactions . . . not involving any public offering" is not defined in the Act2/ or, except in limited circumstances, in the existing rules under the Act. Accordingly, it has been left to Commission interpretations and court decisions to define the scope of the exemption.

The Supreme Court in the Ralston Purina3/ case established the basic criteria to be considered in determining the availability of Section 4(2). The main consideration is whether the offerees need the protection afforded by the Act as evidenced by whether the offerees have "access" to the same kind of information that registration would disclose and whether they are able to fend for themselves. The application of these criteria and other guidelines set forth from time to time by the Commission and the courts has resulted in uncertainty about the availability of the exemption. In addition, some misconceptions have arisen in connection with certain methods used by persons who seek to claim the exemption.

For example, the questions arising under Section 4(2) have generally dealt with what constitutes a non-public offering or a private offering. It has been asserted that an offering to a limited number of persons, not more than twenty-five, for example, does not involve a public offering. This is not by itself an appropriate test. As the Supreme Court stated in Ralston Purina, "the statute would seem to apply to a 'public offering' whether to few or many." 346 U.S. at 125. The Commission continues to be of the opinion that the question is not to be determined exclusively by the number of offerees.

Further, it is frequently asserted that wealthy persons and certain other persons such as lawyers, accountants and businessmen are "sophisticated" investors who do not need the protections afforded by the Act. It is the Commission's view that "sophistication" is not a substitute for access to the same type of information that registration would provide, and that a person's financial resources or sophistication are not, without more, sufficient to establish the availability of the exemption.4/

On the other hand, the Commission is of the view that an offeree need not be an insider such as an officer or director of the issuer in order to have access to information. As a note to the Rule indicates, access can only exist by reason of the offeree's position with respect to the issuer. Position means an employment or family relationship or economic bargaining power that enables an offeree to obtain information from the issuer in order to evaluate the merits and risks of the investment as distinguished from situations where such position does not exist and the issuer voluntarily offers to provide or provides such information.

Moreover, it has been argued that the exemption is established by the issuer merely providing a brochure, or other writing, to the offerees containing the same kind of information that is found in a registration statement. The Commission is of the view that the mere disclosure of the same kind of information that would be contained in a registration statement is not sufficient in itself to establish the availability of an exemption under Section 4(2) of the Act.[5/]

It also has been argued that the private offering exemption can be established where it is represented that the securities are held for investment, where resale is restricted, and where the number of transferees is limited. In this regard, the practice has developed whereby issuers obtain investment letters from purchasers and cause a legend to be imprinted on the face of each certificate restricting transfer. As the Commission and the courts[6/] have previously stated, the signing of an investment letter and the legending of stock certificates are not sufficient to render an offering a private one. Although such precautions should be taken by issuers to protect their claim of exemption by assuring that their purchasers will not in turn distribute securities to others, these are only precautions to prevent illegal distributions and are not, by themselves, to be regarded as a sufficient basis for an exemption from registration for the issuer.

The Commission believes that a rule creating greater certainty in the application of the Section 4(2) exemption is in the public interest for two reasons. First, such a rule should deter reliance on that exemption for offerings of securities to persons who are unable to fend for themselves in terms of obtaining and evaluating information about the issuer and in certain situations, of assuming the risk of investment. These persons need the protections afforded by the registration process. Second, such a rule should reduce uncertainty to the extent feasible and provide more objective standards upon which responsible businessmen may rely in raising capital in a manner that complies with the requirements of the Act.

The Rule is designed to protect investors while at the same time providing more objective standards in order to curtail uncertainty to the extent feasible. In view of the legislative history, statutory language, judicial decisions, and the Commission's reexamination of its interpretations of Section 4(2) of the Act, the Commission is of the view that the significant concepts in determining when transactions are deemed not to involve any public offering are access to the same kind of information that registration would disclose and the ability of offerees to fend for themselves so as not to need the protections afforded by registration.

GENERAL DESCRIPTION

Rule 146 provides that transactions by an issuer involving the offer or sale of its securities shall be deemed not to involve any public offering within the meaning of Section 4(2) of the Act if they are part of an offering that meets all the conditions of the Rule. These conditions relate to limitations on the manner of offering, the nature of the offerees, access to or furnishing of information about the issuer, limitations on the number of purchasers and limitations on the subsequent disposition of securities acquired pursuant to the Rule.

First, in determining whether an offeree needs the protections afforded by registration, it is essential to consider whether the offeree has access to or has been furnished with the same kind of information that registration would disclose as well as an opportunity to acquire additional information necessary to verify that disclosure. Accordingly, conditions relating to information concerning the issuer which must be available to the offeree or his representative are included in the Rule.

Second, in order to assure that the offerees can fend for themselves, the availability of the Rule is conditioned on the nature of the offerees. Thus, the issuer and any person acting on its behalf shall have reasonable grounds to believe, and shall believe, immediately prior to making an offer, either that the offeree has such knowledge and experience that he is capable of evaluating the merits and risks of the proposed investment or that the offeree can bear the economic risk of the investment. In addition, immediately prior to a sale, the issuer and any person acting on its behalf, after making reasonable inquiry, shall have reasonable grounds to believe and shall believe either that the offeree himself has the requisite knowledge and experience, or that the offeree and his offeree representative(s) have such knowledge and experience and that the offeree himself is capable of bearing the economic risk of the investment. The concept of bearing the economic risk of the investment is not inconsistent with the discussion in Ralston Purina about the offeree's ability to fend for himself. The Rule contains special provisions in this regard for offerings in connection with certain types of business combinations.

Third, the Commission believes that there must be limitations on the manner of offering securities pursuant to the exemption to assure that persons to whom such securities are offered have the necessary information available concerning the issuer and can fend for themselves. To assure the non-public manner of the offering, the Rule precludes general advertising or general solicitation, including promotional seminars or meetings in connection with the offering. The Rule would not preclude meetings with certain qualified offerees or with certain other qualified offerees and their offeree representatives to discuss the terms of and to impart information about the offering.

Fourth, the Commission believes that a limitation on the number of purchasers serves to assure that the offering does not involve or result in a deferred distribution. Limitations on the disposition of securities are necessary to assure that the offering does not involve a series of steps resulting in a distribution.

The Rule is only available to issuers of securities and is not available to affiliates of the issuer or other persons for sales of the issuer's securities. Persons who acquire securities from issuers in transactions

complying with the Rule acquire securities that are restricted in that they can be reoffered and resold only if registered under the Act or pursuant to an exemption from such registration provisions. In this connection, Rule 144 under the Act provides objective standards for the public resale of restricted securities. (See Securities Act Release No. 5223). Rule 146 has been adopted in the context of , and in conjunction with, several rules, amendments to rules and forms, and releases which the Commission has recently adopted or issued including:

1. Rule 144 under the Act (Securities Act Release No. 5223), as amended (Securities Act Release No. 5307 and Securities Act Release No. 5452);

2. Rule 145 under the Act (Securities Act Release No. 5316);

3. Adoption of Form S-16 under the Act for securities offered in certain specified transactions (Securities Act Release No. 5117) and adoption of amendments to Form S-16 to liberalize the conditions under which the form could be used (Securities Act Release No. 5265);

4. Amendments to Regulation A under Section 3(b) of the Act (Securities Act Release No. 5225);

5. Publication of a release relating to the use of legends and stop-transfer instructions as evidence of non-public offerings (Securities Act Release No. 5121);

6. Publication of a release relating to the applicability of the anti-fraud provisions of the Securities Act to certain practices in connection with transactions by issuers and others not involving public offerings (Securities Act Release No. 5226);

7. Amendments to Forms 10-K and 10-Q under the Securities Exchange Act of 1934 (Exchange Act) to require disclosure of securities sold pursuant to Section 4(2) of the Act (Securities Exchange Act Release No. 9443);

8. Adoption of Rule 15c2-11 under the Exchange Act which requires that dealers have adequate information available concerning any issuer in whose securities they make a market (Securities Exchange Act Release No. 9310);

9. Adoption of amendments to Form 10-K to require more meaningful disclosure in reports on that Form (Securities Exchange Act Release No. 10180).

SYNOPSIS OF THE PROVISIONS OF RULE 146

Preliminary Notes

Preliminary Notes to the Rule briefly describe the Rule and make clear that all transactions which are applying traditional integration standards part of an offering must meet all the conditions of the Rule for it to be available. The Preliminary Notes also emphasize that compliance with all the conditions of the Rule is not the exclusive means of establishing an exemption pursuant to Section 4(2) of the Act, that attempted compliance with Rule 146 does not act as an election, that the Rule does not relieve issuers from requirements of state securities laws, and that the Rule is an

issuer's rule only. Another Preliminary Note makes clear that, for purposes of the Rule, clients of an investment adviser, customers of a broker or dealer, trusts administered by a bank trust department or persons with similar relationships will be considered to be the "offerees" or "purchasers," regardless of the amount of discretionary authority held by such investment adviser, broker or dealer, bank trust department, or other person. In addition, the Preliminary Notes restate the Commission's position, as with respect to Rules 144 and 147, that this Rule is not available to any issuer with respect to any transactions which, although in technical compliance with the Rule, are part of a plan or scheme to evade the registration provisions of the Act. In such cases registration pursuant to the Act is required.

Rule 146(a): Definitions

Offeree Representative: Rule 146(a)(1)

The term "offeree representative" is defined in subparagraph (a)(1) of the Rule as a person who the issuer and any person acting on its behalf have, after making reasonable inquiry, reasonable grounds to believe and believe is not an affiliate, director, officer or other employee, or beneficial owner of 10 percent or more of the equity of the issuer (except when the offeree is a specified relative of such person or a trust or organization with which such person and/or such relative has a specified relationship) (subdivision (i)); has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment (subdivision (ii)); is acknowledged, in writing, by the offeree during the course of the transaction to be his offeree representative (subdivision (iii)); and discloses to the offeree, in writing, any material relationship existing or mutually understood to be contemplated between himself or his affiliates and the issuer or its affiliates or any such relationship which existed during the previous two years, and any compensation received as a result of such relationship (subdivision (iv)). As was noted in the release accompanying the rule as proposed for comment in October 1973, the acknowledgment and disclosure of relationships must be made with respect to each prospective investment even in the case of a discretionary account. Where an adviser with discretionary authority wants to act as offeree representative, the Rule requires that the acknowledgment specified in subdivision (a)(1)(iii) of the Rule be obtained for each transaction. Accordingly, advance blanket acknowledgement for "all securities transactions" or "all private placements" or similar broad advance acknowledgments will not satisfy the Rule. This is particularly important, since the offeree representative is required by subdivision (a)(1)(iv) of the Rule to disclose to the offeree, in writing, any material relationships between the adviser and the issuer. This disclosure is required in connection with each offering pursuant to the Rule in order that the offeree be given an opportunity to consider any conflicts of interest the adviser may have prior to acknowledging the adviser as his offeree representative for the particular offering. A note has been added to the offeree representative definition making clear that where an offeree representative or its affiliates has a material relationship with the issuer or its affiliates, disclosure of such relationship does not relieve the offeree representative of its obligation to act in the interest of the offeree.

Several changes were made from the rule as last proposed. As proposed in October 1973, no affiliate, associate or employee of the issuer could be an offeree representative, except in specified situations; as adopted, the term "associate" has been deleted, but the definition now precludes officers and directors of the issuer, as well as 10 percent stockholders, from being offeree representatives, except in specified situations. In addition, the adopted Rule requires disclosure of any material relationship between the offeree representative or its affiliates and the issuer or its affiliates. The qualifier "material" is new to the Rule (and is defined in subparagraph (a)(4)) and disclosure of relationships with affiliates of the offeree representative is also new. The Rule also makes clear that an offeree can have more than one offeree representative. A note has been added reminding persons to consider the applicability of the Exchange Act and the Investment Advisers Act of 1940.

Issuer: Rule 146(a)(2)

For purposes of the Rule the definition of issuer in Section 2(4) of the Act applies. However, subparagraph (a)(2) includes a definition of "issuer" for purposes of offerings of certain securities in connection with proceedings under the Bankruptcy Act. The rule as proposed in October 1973 contained a definition of issuer for certain offerings involving partnerships. This has been deleted from the Rule as adopted because it was ambiguous and the Commission determined that Rule 146 was not the appropriate place to deal with that question at this time.

Affiliate: Rule 146(a)(3)

A definition of "affiliate", similar to that in Rule 144 under the Act, has been added to the Rule.

Material: Rule 146(a)(4)

A definition of "material" as it relates to the "material relationships" that must be disclosed by the offeree representative (subparagraph (a)(1)) and by the issuer (subparagraph (e)(3)) has been added to make clear that materiality is to be determined from the reasonable investor's point of view and not through some formula measuring the importance of the transaction to the offeree representative or the issuer. The definition is based on that used by the Supreme Court in Affiliated Ute Citizens of Utah v. United States (406 U.S. 128, 154, 1972).

Deletion of Proposed Rule 146(a)(2): Direct Communication

The term "direct communication" has been deleted from the Rule, although the substantive requirement of an opportunity for the offeree or his offeree representative to ask questions of, and receive answers from, the issuer or a person acting on its behalf, has been retained. The requirement is now part of paragraph (e), "Access to or Furnishing of Information."

Deletion of Proposed Rule 146(a)(3): Executive Officer

The definition of executive officer has been deleted from the definition section of the Rule because the term no longer appears in paragraph (g) of the Rule. The exclusion of "executive officers" from the count of thirty-five purchasers in a twelve month period is not necessary since the twelve month period has been abandoned as explained under paragraphs (b) and (g).

Rule 146(b): Conditions to be Met

Paragraph (b) of the Rule provides that transactions by an issuer involving the offer, offer to sell, offer for sale, or sale of securities of the issuer that are part of an offering that is made in accordance with all the conditions of the Rule are deemed to be transactions not involving any public offering within the meaning of Section 4(2) of the Act.

The Rule does not define "offering", as stated in the Preliminary Notes. In most cases, the traditional integration standards, as set forth in the Preliminary Notes, would have to be applied in order to determine what offers, offers to sell, offers for sale, and sales are part of an offering. The Rule, as adopted, does contain a safe harbor provision similar to that in Rule 147. In general, for purposes of the Rule only, an offering will be deemed not to include any offers, offers to sell, offers for sale or sales of securities of the issuer that take place prior to the six month period immediately preceding or after the six month period immediately following any offers, offers for sale, or sales pursuant to Rule 146, if during both of said six month periods there were no offers or sales of securities by or for the issuer of the same or similar class as those offered or sold pursuant to the Rule. If there were offers or sales during the six month periods before or after the offering pursuant to the Rule, the traditional integration factors set forth in Preliminary Note 3 would have to be looked to for guidance as to whether or not those offers or sales would be integrated with those made pursuant to the Rule. This concept of offering also relates specifically to the limitation on number of purchasers in paragraph (g) since that condition has been revised to limit to thirty-five the number of purchasers in any offering, as opposed to in any twelve month period, as proposed.

Rule 146(c): Limitations on Manner of Offering

Paragraph (c) of the Rule specifies limitations on the manner in which the securities can be offered and sold. The Rule prohibits the issuer or any person acting on its behalf from offering or selling the securities through any form of general advertising or general solicitation including, but not limited to advertisements or other communication in newspapers, magazines, or other media; broadcasts on radio or television; seminars or promotional meetings or any letter, circular, or other written communication.

The prohibition on general advertising and general solicitation does not necessarily mean that there can be no meetings or written communication. It means that any such meetings can involve only offerees and their offeree representatives who can satisfy the conditions of paragraph (d), "Nature of Offerees," and that any written material can be distributed only to offerees who satisfy the conditions of paragraph (d) and only if such communications contain an undertaking to provide the information specified in subparagraph (e)(1) on request. Of course, any person acting on behalf of the issuer can attend such meetings or seminars without satisfying the conditions of paragraph (d), assuming that he is not and will not become an offeree. The substance of the requirement that there be direct communication has been moved from paragraph (c) of the Rule to paragraph (e), "Access to and Furnishing of Information."

Rule 146(d): Nature of Offerees

Subparagraph (d)(1) of the Rule requires that the issuer and any person acting on its behalf shall have reasonable grounds to believe and shall believe immediately prior to making an offer either that the offeree has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or that an offeree can bear the economic risk of the investment. Subparagraph (d)(2) requires that immediately prior to making a sale, the issuer and any person acting on its behalf, after making reasonable inquiry, shall have reasonable grounds to believe and shall believe either (1) that the offeree has the requisite knowledge and experience, or (2) that the offeree and his offeree representative(s) have the requisite knowledge and experience and that the offeree is a person who is able to bear the economic risk of the investment.

The Commission has determined to retain the economic risk test for offerees who need the knowledge and experience of an offeree representative in order to be qualified purchasers. This is necessary in order to control the types of persons to whom offers can be made. The Commission believes that the determination of "ability to bear the economic risk" will vary with the circumstances. Important considerations are whether the offeree could afford to hold unregistered securities for an indefinite period, and whether, at the time of the investment, he could afford a complete loss.

The structure of subparagraphs (d)(1) and (d)(2) has been changed from the rule as proposed so that the sequence of events is clearer. The substance, however, is not significantly different. In addition, the requirement that the issuer make reasonable inquiry as to the offeree's qualifications prior to sale to the offeree has been made explicit. If, as a result of inquiry after the offer, but before the sale, or otherwise, the issuer discovers that the offeree was not qualified, the Rule is still available as to the offer if the issuer had reasonable grounds to believe and believed, immediately prior to making the offer, that the offeree was qualified.

The same would be true if it is discovered after a sale that the purchaser did not in fact meet the standards of subparagraph (d)(2), as long as the issuer had had reasonable grounds to believe, and had believed, that the offeree met the standards of subparagraph (d)(1) and, after making reasonable inquiry, that he met the standards of subparagraph (d)(2). The rule as proposed contained a subparagraph (d)(3) which was an attempt to clarify the above point. However, subparagraph (d)(3) has been deleted because it was extraneous.

Rule 146(e): Access to or Furnishing of Information

Paragraph (e) of the Rule requires that the offeree have access to the same kind of information that is required by Schedule A of the Act to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense (subdivision (e)(1)(i)) or that the offeree or his offeree representative be furnished, during the course of the transaction and prior to sale, such information (subdivision (e)(1)(ii)). The term "access" is used in the Rule in the same sense that it has been used by courts and the Commission in the past--to refer to the offeree's position with respect to the issuer. This position can only exist because of an employment or family relationship or economic bargaining power that enables a person to obtain information from the issuer in order to evaluate the merits and risks of the prospective investment. A note to the Rule reflects the foregoing.

In addition, the offeree or his offeree representative must have available to him the opportunity to obtain any additional information necessary to verify the accuracy of the information obtained pursuant to subparagraph (e)(1) to the extent the issuer possesses such information or can acquire it without unreasonable effort or expense (subparagraph (e)(2)). The direct communication requirement in paragraph (c) of the rule as proposed was incorporated in substance into subparagraph (e)(2) where it is more relevant. Such verification and opportunity for communication are appropriate in view of the absence of the statutory safeguards and sanctions attendant to the registration process, as well as the absence of traditional underwriter's due diligence. An explanatory note to this paragraph makes clear that information need not be continued to be furnished nor the opportunities for verification continued with respect to those offerees who have indicated that they are not interested in purchasing the securities offered, or to those to whom the issuer or any person acting on its behalf has determined not to sell (except where an undertaking was made pursuant to subparagraph (c)(3)).

In order to provide standards for the types of information that would satisfy the conditions of subdivision (e)(1)(ii), the Rule has been revised to specify more meaningfully the information required to be furnished by reporting and non-reporting issuers. An issuer subject to the reporting provisions of the Exchange Act may satisfy the provisions of subdivision (e)(1)(ii) by providing each offeree or his representative with the information contained in the annual report required to be filed under that Act or in a registration statement on Form S-1 under the Act, or on Form 10 under the Exchange Act, whichever is the most recent required to be filed. In addition, the issuer must provide the information contained in any

definitive proxy statement required to be filed, and in any reports or documents required to be filed by the issuer in compliance with Section 13 or 15(d) of the Exchange Act, since the filing of the annual report or registration statement. The issuer must also provide each offeree with a brief description of the securities being offered, the intended use of proceeds and any material changes in the issuer's affairs not disclosed in the forms filed. The Rule permits the information to be provided to offerees in one document, such as an offering circular, since the combined document may make the information more readily understandable.

Non-reporting issuers may satisfy subdivision (e)(1)(ii) by providing the information specified by the registration statement form which the issuer would be entitled to use, except that where certified financial statements are not available and cannot be obtained without unreasonable effort or expense, they may be provided on an unaudited basis.

A new subdivision of the Rule, (e)(1)(ii)(c), provides that exhibits required to be filed with registration statements and reports need not be given to the offeree or his representative as long as such exhibits are described and are available for inspection pursuant to subparagraph (e)(2).

Subparagraph (e)(3) requires, as it did in the proposal, that the issuer or any person acting on its behalf inform each offeree prior to sale and in writing, of the need to bear the economic risk of investment because the securities are not registered and of the restrictions on resale. In addition, the Rule now requires that the issuer or any person acting on its behalf disclose to each offeree, prior to sale, in writing, any material relationship between the offeree's offeree representative or its affiliates and the issuer or its affiliates of the type described in subdivision (a)(1)(iv). This additional requirement has been added because of the importance of this disclosure and because the burden for complying with the Rule must ultimately rest on the issuer.

Rule 146(f): Business Combinations

Paragraph (f) of the Rule on business combinations has been substantially revised in form, although the substance is similar to that in the rule as last proposed for comment. Instead of including a definition of "business combination" in the rule itself, the Rule now refers to any transaction of the type described in paragraph (a) of Rule 145. The Rule 145 definition of business combination does not include an exchange offer although the October 1973 Rule 146 proposal did. In an exchange offer the issuer has a choice of offerees and, therefore, does not need the special provisions of paragraph (f).

Subparagraph (f)(2) of the Rule provides that paragraph (d) of the Rule, "Nature of Offerees," does not apply to business combinations, but subparagraph (f)(3) goes on to require that the issuer and any person acting on its behalf, after making reasonable inquiry, shall have reasonable grounds to believe and shall believe, prior to the submission of any plan for a business combination to security holders for their approval, that each offeree alone or with his offeree representative(s) has the requisite knowledge and experience. Subparagraph (f)(3) means that an offeree who needs an offeree representative in order to satisfy the knowledge and experience test, and who refuses to have one, may make the Rule unavailable for the transaction. Numerous comments on this point were received in response to a similar condition in the rule as last proposed. Although the Commission is aware of the possible problems this may cause, the Commission does not believe that it can allow satisfaction of the state corporate law requirements as to business combinations to replace satisfaction of the federal securities laws. The Rule has been revised, however, to provide that subparagraph (h)(4), which requires a written agreement from the purchaser that the securities will not be sold without registration or an exemption therefrom, will not apply to business combinations because of the difficulty of obtaining such an agreement in some cases where the purchasers are a group over which the issuer has no control. The securities acquired are restricted, however, in the same manner as other securities acquired pursuant to the Rule, and the issuer, for its own protection, should consider obtaining appropriate letters. The Rule also provides that the issuer must, in connection with the information furnished pursuant to subparagraph (e)(3), inform each offeree in writing about any terms of the transaction relating to any security holder that are not proposed to be identical to those relating to all other security holders (subparagraph (f)(4)).

The rule as proposed contained a provision that certain written communications would be deemed not to be "offers" for purposes of a business combination. We have deleted this provision since we believe it is no longer relevant in view of new subparagraph (f)(3).

Rule 146(g): Number of Purchasers

The Rule as last proposed provided that in any consecutive twelve month period there could be no more than thirty-five persons who purchased securities of the issuer of the same or similar class pursuant to the rule, or otherwise in reliance on Section 4(2). The proposed rule also set forth various classes of purchasers who would not be included in counting the thirty-five. The Commission has decided that the thirty-five purchasers

in twelve month test is too rigid and involves too many exceptions to be useful. In addition, it would have made it difficult for an issuer to know when the rule was available since it would have had to wait twelve months after every sale. Therefore, as described under Rule 146(b), "Conditions to Be Met," the Rule is now based on the traditional concept of "an offering" and subparagraph (g)(1) now requires that there be no more than thirty-five purchasers in any offering pursuant to the Rule. In order to determine what constitutes "an offering," reference would have to be made to the traditional integration standards, as set forth in a Preliminary Note. In addition, subparagraph (b)(1) of the Rule provides a safe harbor for certain offers and sales. Reliance on the traditional integration standards means that the various exclusions for directors and officers, bank lenders, subsidiaries, employee plans and business combinations are no longer necessary. The specific exclusions were only necessary when all sales of the same or similar class of securities during a twelve month period were automatically integrated.

In the Rule as adopted there are specific provisions for calculating the thirty-five purchasers. Subdivision (g)(2)(i) of the Rule, as adopted, indicates that for purposes of computing the number of purchasers, some purchasers would be excluded: certain relatives of a purchaser, trusts and estates in which the purchaser and such relatives own all of the beneficial interest and corporations or other organizations in which the purchaser and such relatives are beneficial owners of all of each class of equity securities or all of the equity interest. As in the rule as last proposed, for purposes only of counting the number of purchasers, those who purchase or agree in writing to purchase, for cash in a single payment or installments, securities for $150,000 or more would be excluded. However, the issuer would have to satisfy all the other provisions of the Rule with respect to such persons.

Subdivision (g)(2)(ii) provides that corporations, partnerships, trusts and certain other entities will be counted as one purchaser unless the entity was formed for the specific purpose of acquiring the securities offered, in which case each beneficial owner of an equity interest in the entity would be counted as a separate purchaser.

The rule as proposed would have treated clients of an investment adviser as separate persons in determining the number of persons to whom securities could be sold, regardless of the amount of discretion given to the investment adviser to act on behalf of the client in purchasing securities. The Commission received many comments suggesting that an investment adviser, broker-dealer or trust department that purchases securities for discretionary or advisory accounts should count as only one person for purposes of the Rule. Having reviewed the comments and considered the matter, the Commission still believes that, in order to avoid the possibility of a

distribution, it is necessary to count each purchaser as a separate person for purposes of paragraph (g). This position is now set forth in Preliminary Note 5, discussed above. In determining the number of purchasers in an offering pursuant to the Rule each client of an investment adviser, each customer of a broker-dealer and each trust administered by a bank trust department will be counted as a separate purchaser. Pursuant to subdivision (g)(2)(ii), investment companies or pension or other trusts will be counted as one purchaser. However, each trust or investment company or group of trusts or investment companies under common management will be treated as a separate purchaser.

Rule 146(h): Limitations on Disposition

The Rule also provides that the issuer and any person acting on its behalf must take reasonable care to assure that the purchasers are not underwriters. Such reasonable care shall include but is not necessarily limited to (1) making reasonable inquiry to determine if the purchaser is purchasing for his own account or on behalf of others; (2) placing a legend on the certificates or other documents evidencing the securities indicating that they were not registered and setting forth or referring to the restrictions on transferability and sale; (3) issuing stop transfer instructions to the transfer agent, if any, or making an appropriate notation in the issuer's records if the issuer transfers its own securities; and (4) except as provided in subparagraph (f)(2), obtaining a written agreement from the purchaser that the securities will not be resold without registration or exemption therefrom. The Commission believes that these limitations are necessary in order to protect the public from a deferred distribution. They are also in the self interest of the issuer.

Deletion of Proposed Rule 146(i): Report of Sale

The Commission has decided to delete the requirement that a report of sales made pursuant to Rule 146 be filed on Form 146. As the rule was last proposed, a report of sales had to be filed within 45 days after the end of any quarter of the issuer's fiscal year during which certain sales were effected pursuant to the proposed Rule. The Commission has determined that requiring the filing of such a Form as a condition of the Rule would unnecessarily increase the difficulty of complying with the Rule for many small issuers. In addition, filing requirements would generally affect only non-public companies, since public companies already supply similar information in their Form 10-Q and Form 10-K filings under the Exchange Act. The Commission will reexamine the need for a filing requirement after experience with the Rule has been gained, and if appropriate for the protection of investors and in the public interest, will propose amendments to the Rule to require such form.

OPERATION OF RULE 146

The Rule will operate prospectively only starting from its effective date, June 10, 1974. Further, the staff will issue interpretive letters to assist persons in complying with the Rule. Although the staff will continue to consider no-action requests relating to Section 4(2) of the Act, such letters will only be issued infrequently and only in the most compelling circumstances.

The Commission recognizes that no one rule can adequately cover all legitimate private offerings and sales of securities. It is to be emphasized that the Rule does not provide the exclusive means for offering and selling securities in reliance on Section 4(2). Issuers who satisfy the criteria set forth in relevant judicial and administrative interpretations of Section 4(2) in effect at the time of a proposed transaction may offer and sell without compliance with the Rule. In addition, it should be noted that attempted compliance with Rule 146 does not act as an election so that the issuer can always claim the protection of both the Rule and Section 4(2), but will have the burden of proving the availability of the exemption.

The courts and the Commission have consistently held that one claiming an exemption under Section 4(2) of the Act has the burden of proving that the exemption is available to him and the Rule does not shift that burden. In addition, it should be pointed out that the burden of proof applies with respect to each offeree and not just to the purchasers of the securities. See Lively v. Hirschfeld, 440 F. 2d 631 (10th Cir. 1971). Accordingly, any issuer who relies on the Rule has the burden of establishing that it has satisfied all the conditions of the Rule. Such issuer for its own protection should obtain and retain in its files written evidence that would assist in meeting this evidentiary burden.

The Commission has determined not to include within the terms and conditions of Rule 146 specific standards for determining whether a private offering should be regarded as a part of a larger public offering for which the exemption provided by Section 4(2) would not be available. The Commission rather has determined that its existing guidelines relating to integration of offerings as set forth in Securities Act Release No. 4552 7/ should apply to offerings made pursuant to Rule 146. The Commission believes that the following factors discussed in that Release are relevant to the question of integration: whether (1) the offerings are part of a single plan of financing, (2) the offerings involve issuance of the same class of security, (3) the offerings are made at or about the same time, (4) the same type of consideration is to be received, and (5) the offerings are made for the same general purpose.

In view of the objectives and policies underlying the Act, the Rule is not available to any issuer with respect to any transaction which, although in technical compliance with the provisions of the Rule, is part of a plan or scheme to evade the registration provisions of the Act. In such case, registration is required.

Rule 146 relates to transactions exempted by Section 4(2) of the Act from the registration provisions of Section 5; it does not provide an exemption from the anti-fraud provisions of the securities laws or the civil liabilities provisions of Section 12(2) of the Act or other provisions of the securities laws. In addition, investment companies or persons acting on their behalf proposing to offer or sell securities in reliance on the Rule should carefully consider all applicable provisions of the Investment Company Act of 1940 before proceeding.

The Rule is available only to the issuer of the securities and not to affiliates or other persons reselling or otherwise disposing of securities of the issuer. Such disposition must be made in compliance with the registration provisions of the Act unless an exemption from such provisions is available. Also, the Rule does not relieve issuers of their obligations under relevant state laws.

It should be recognized that the Rule is intended to be in the nature of an experiment and that the Commission will observe its operation to determine whether it is consistent with the objectives of the Act. If experience with the proposed Rule indicates that it is not operating for the protection of investors or in the public interest, it will be rescinded or appropriately amended.

The Commission hereby adopts Rule 146 pursuant to Sections 4(2) and 19(a) of the Securities Act of 1933, as amended, effective June 10, 1974 for offerings commencing on or after that date. The Commission finds that the changes reflected in the Rule as adopted, from the rule as last proposed for comment, are technical or generally have already been subject to public comment, and that further notice and other rule making procedures pursuant to the Administrative Procedure Act are not necessary.

The text of Rule 146 is attached hereto.

By the Commission.

George A. Fitzsimmons
Secretary

1/ H.R. Rep. No. 85, 73rd Cong., 1st Sess. 5 (1933).

2/ The House Report does indicate that the exemption was originally intended to permit an issuer to make a specific or isolated sale of its securities to a particular person or financial institution. Id. at p. 15-16.

3/ SEC v. Ralston Purina Co., 346 U.S. 119 (1953).

4/ United States v. Custer Channel Wing Corp., 376 F. 2d 675 (4th Cir. 1967); SEC v. Tax Service, Inc., 357 F. 2d 143 (4th Cir. 1966).

5/ See SEC v. Continental Tobacco Company of South Carolina, Inc., 463 F. 2d 137 (5th Cir. 1972); Hill York Corp. v. Freeman, 448 F. 2d 680 (5th Cir. 1971).

6/ Securities Act Release No. 5121 (December 30, 1970); United States v. Custer Channel Wing, 376 F. 2d 675 (4th Cir. 1967).

7/ Issued November 6, 1962.

Rule 146. Transactions by an Issuer Deemed Not to Involve Any Public Offering

Preliminary Notes

1. The Commission recognizes that no one rule can adequately cover all legitimate private offers and sales of securities. Transactions by an issuer which do not satisfy all of the conditions of this rule shall not raise any presumption that the exemption provided by Section 4(2) of the Act is not available for such transactions. Issuers wanting to rely on that exemption may do so by complying with administrative and judicial interpretations in effect at the time of the transactions. Attempted compliance with this rule does not act as an election; the issuer can also claim the availability of Section 4(2) outside the rule.

2. Nothing in this rule obviates the need for compliance with any applicable state law relating to the offer and sale of securities.

3. Section 5 of the Act requires that all securities offered by the use of mails or other channels of interstate commerce be registered with the Commission. Congress, however, provided certain exemptions in the Act from such registration provisions where there was no practical need for registration or where the public benefits of registration were too remote. Among these exemptions is that provided by Section 4(2) of the Act for transactions by an issuer not involving any public offering. The courts and the Commission have interpreted the Section 4(2) exemption to be available for offerings to persons who have access to the same kind of information that registration would provide and who are able to fend for themselves. The indefiniteness of such terms as "public offering", "access" and "fend for themselves" has led to uncertainties with respect to the availability of the Section 4(2) exemption. Rule 146 is designed to provide, to the extent feasible, objective standards upon which responsible businessmen may rely in raising capital under claim of the Section 4(2) exemption and also to deter reliance on that exemption for offerings of securities to persons who need the protections afforded by the registration process.

In order to obtain the protection of the rule, all its conditions must be satisfied and the issuer claiming the availability of the rule has the burden of establishing, in an appropriate forum, that it has satisfied them. The burden of proof applies with respect to each offeree as well as each purchaser. See Lively v. Hirschfeld, 440 F. 2d 631 (10th Cir. 1971). Broadly speaking, the conditions of the rule relate to limitations on the manner of the offering, the nature of the offerees, access to or furnishing of information, the number of purchasers, and limitations on disposition.

The term "offering" is not defined in the rule. The determination as to whether offers, offers to sell, offers for sale, or sales of securities are part of an offering (i.e., are deemed to be "integrated") depends on the particular facts and circumstances. See Securities Act Release No. 4552 (November 6, 1962). All offers, offers to sell, offers for sale, or sales which are part of an offering must meet all of the conditions of Rule 146 for the rule to be available. Release 33-4552 indicates that in determining whether offers and sales should be regarded as a part of a larger offering and thus should be integrated, the following factors should be considered:

(a) whether the offerings are part of a single plan of financing;

(b) whether the offerings involve issuance of the same class of security;

(c) whether the offerings are made at or about the same time;

(d) whether the same type of consideration is to be received; and

(e) whether the offerings are made for the same general purpose.

4. Rule 146 relates to transactions exempted from Section 5 by Section 4(2) of the Act. It does not provide an exemption from the anti-fraud provisions of the securities laws or the civil liability provisions of Section 12(2) of the Act or other provisions of the securities laws, including the Investment Company Act of 1940.

5. Clients of an investment adviser, customers of a broker or dealer, trusts administered by a bank trust department or persons with similar relationships shall be considered to be the "offerees" or "purchasers" for purposes of the rule regardless of the amount of discretion given to the investment adviser, broker or dealer, bank trust department or other person to act on behalf of the client, customer or trust.

6. The rule is available only to the issuer of the securities and is not available to affiliates or other persons for sales of the issuer's securities.

7. Finally, in view of the objectives of the rule and the purposes and policies underlying the Act, the rule is not available to any issuer with respect to any transactions which, although in technical compliance with the rule, are part of a plan or scheme to evade the registration provisions of the Act. In such cases registration pursuant to the Act is required.

(a) Definitions. The following definitions shall apply for purposes of this rule.

(1) Offeree Representative. The term "offeree representative" shall mean any person or persons, each of whom the issuer and any person acting on its behalf, after making reasonable inquiry, have reasonable grounds to believe and believe satisfies all of the following conditions:

(i) is not an affiliate, director, officer or other employee of the issuer, or beneficial owner of 10 percent or more of any class of the equity securities or 10 percent or more of the equity interest in the issuer, except where the offeree is:

(a) related to such person by blood, marriage or adoption, no more remotely than as first cousin;

(b) any trust or estate in which such person or any persons related to him as specified in subdivision (a) or (c) collectively have 100 percent of the beneficial interest (excluding contingent interests) or of which any such person serves as trustee, executor, or in any similar capacity; or

(c) any corporation or other organization in which such person or any persons related to him as specified in subdivision (a) or (b) collectively are the beneficial owners of 100 percent of the equity securities (excluding directors' qualifying shares) or equity interest;

(ii) has such knowledge and experience in financial and business matters that he, either alone, or together with other offeree representatives or the offeree, is capable of evaluating the merits and risks of the prospective investment:

(iii) is acknowledged by the offeree, in writing, during the course of the transaction, to be his offeree representative in connection with evaluating the merits and risks of the prospective investment; and

(iv) discloses to the offeree, in writing, prior to the acknowledgement specified in subdivision (iii), any material relationship between such person or its affiliates and the issuer or its affiliates, which then exists or is mutually understood to be contemplated or which has existed at any time during the previous two years, and any compensation received or to be received as a result of such relationship.

NOTE 1: Persons acting as offeree representatives should consider the applicability of the registration and anti-fraud provisions relating to brokers and dealers under the Securities Exchange Act of 1934 and relating to investment advisers under the Investment Advisers Act of 1940.

NOTE 2: The acknowledgment required by subdivision (iii) and the disclosure required by subdivision (iv) must be made with specific reference to each prospective investment. Advance blanket acknowlegment, such as for "all securities transactions" or "all private placements", is not sufficient.

NOTE 3: Disclosure of any material relationships between the offeree representative or its affiliates and the issuer or its affiliates does not relieve the offeree representative of its obligation to act in the interest of the offeree.

(2) Issuer. The definition of the term "issuer" in Section 2(4) of the Act shall apply, provided that notwithstanding that definition, in the case of a proceeding under the Bankruptcy Act, the trustee, receiver, or debtor in possession shall be deemed to be the issuer in an offering for purposes of a plan of reorganization or arrangement, if the securities offered are to be issued pursuant to the plan, whether or not other like securities are offered under the plan in exchange for securities of, or claims against, the debtor.

(3) Affiliate. The term "affiliate" of a person means a person that directly or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with such person.

(4) Material. The term "material" when used to modify "relationship" means any relationship that a reasonable investor might consider important in the making of the decision whether to acknowledge a person as his offeree representative.

(b) Conditions to be Met. Transactions by an issuer involving the offer, offer to sell, offer for sale or sale of securities of the issuer that are part of an offering that is made in accordance with all the conditions of this rule shall be deemed to be transactions not involving any public offering within the meaning of Section 4(2) of the Act.

(1) For purposes of this rule only, an offering shall be deemed not to include offers, offers to sell, offers for sale or sales of securities of the issuer pursuant to the exemptions provided by Section 3 or Section 4(2) of the Act or pursuant to a registration statement filed under the Act, that take place prior to the six month period immediately preceding or after the six month period immediately following any offers, offers for sale or sales pursuant to this rule, provided, that there are during neither of said six month periods any offers, offers for sale or sales of securities by or for the issuer of the same or similar class as those offered, offered for sale or sold pursuant to the rule.

NOTE: In the event that securities of the same or similar class as those offered pursuant to the rule are offered, offered for sale or sold less than six months prior to or subsequent to any offer, offer for sale or sale pursuant to the rule, see Preliminary Note 3 hereof as to which offers, offers to sell, offers for sale or sales may be deemed to be part of the offering.

(c) Limitations on Manner of Offering. Neither the issuer nor any person acting on its behalf shall offer, offer to sell, offer for sale, or sell the securities by means of any form of general solicitation or general advertising, including but not limited to, the following:

(1) Any advertisement, article, notice or other communication published in any newspaper, magazine or similar medium or broadcast over television or radio;

(2) Any seminar or meeting, except that if subparagraph (d)(1) is satisfied as to each person invited to or attending such seminar or meeting, and, as to persons qualifying only under subdivision (d)(1)(ii), such persons are accompanied by their offeree representative(s), then such seminar or meeting shall be deemed not to be a form of general solicitation or general advertising; and

(3) Any letter, circular, notice or other written communication, except that if subparagraph (d)(1) is satisfied as to each person to whom the communication is directed and the communication contains an undertaking to provide the information specified by subparagraph (e)(1) on request, such communication shall be deemed not to be a form of general solicitation or general advertising.

(d) Nature of Offerees. The issuer and any person acting on its behalf who offer, offer to sell, offer for sale or sell the securities shall have reasonable grounds to believe and shall believe:

(1) immediately prior to making any offer, either:

(i) that the offeree has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or

(ii) that the offeree is a person who is able to bear the economic risk of the investment

; and

(2) immediately prior to making any sale, after making reasonable inquiry, either:

(i) that the offeree has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or

(ii) that the offeree and his offeree representative(s) together have such knowledge and experience in financial and business matters that they are capable of evaluating the merits and risks of the prospective investment and that the offeree is able to bear the economic risk of the investment.

(e) Access to or Furnishing of Information.

NOTE: Access can only exist by reason of the offeree's position with respect to the issuer. Position means an employment or family relationship or economic bargaining power that enables the offeree

to obtain information from the issuer in order to evaluate the merits and risks of the prospective investment.

(1) Either

(i) each offeree shall have access during the course of the transaction and prior to the sale to the same kind of information that is specified in Schedule A of the Act, to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense; or

(ii) each offeree or his offeree representative(s), or both, shall have been furnished during the course of the transaction and prior to sale, by the issuer or any person acting on its behalf, the same kind of information that is specified in Schedule A of the Act, to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense. This condition shall be deemed to be satisfied as to an offeree if the offeree or his offeree representative is furnished with information, either in the form of documents actually filed with the Commission or otherwise, as follows:

(a) in the case of an issuer that is subject to the reporting requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934:

(1) the information contained in the annual report required to be filed under the Exchange Act or a registration statement on Form S-1 under the Act or on Form 10 under the Exchange Act, whichever filing is the most recent required to be filed, and the information contained in any definitive proxy statement required to be filed pursuant to Section 14 of the Exchange Act and in any reports or documents required to be filed by the issuer pursuant to Section 13(a) or 15(d) of the Exchange Act, since the filing of such annual report or registration statement, and

(2) a brief description of the securities being offered, the use of the proceeds from the offering, and any material changes in the issuer's affairs which are not disclosed in the documents furnished;

(b) in the case of all other issuers, the information that would be required to be included in a registration statement filed under the Act on the form which the issuer would be entitled to use, provided, however, that if the issuer does not have the audited financial statements required by such form and cannot obtain them without unreasonable effort or expense, such financial statements may be provided on an unaudited basis;

(c) notwithstanding subdivisions (e)(1)(ii)(a) and (b) exhibits required to be filed with the Commission as part of a registration statement or report need not be furnished to each offeree or offeree representative if the contents of the exhibits are identified and such exhibits are available pursuant to subparagraph (e)(2)

; and

(2) The issuer shall make available, during the course of the transaction and prior to sale, to each offeree or his offeree representative(s) or both, the opportunity to ask questions of, and receive answers from, the issuer or any person acting on its behalf concerning the terms and conditions of the offering and to obtain any additional information, to the extent the issuer possesses such information or can acquire it without unreasonable effort or expense, necessary to verify the accuracy of the information obtained pursuant to subparagraph (e)(1) above; and

(3) The issuer or any person acting on its behalf shall disclose to each offeree, in writing, prior to sale:

(i) any material relationship between his offeree representative(s) or its affiliates and the issuer or its affiliates, which then exists or mutually is understood to be contemplated or which has existed at any time during the previous two years, and any compensation received or to be received as a result of such relationship;

(ii) that a purchaser of the securities must bear the economic risk of the investment for an indefinite period of time because the securities have not been registered under the Act and, therefore, cannot be sold unless they are subsequently registered under the Act or an exemption from such registration is available; and

(iii) the limitations on disposition of the securities set forth in subparagraphs (h)(2), (h)(3), and (h)(4) of the rule

NOTE: Information need not be provided and opportunity to obtain additional information need not be continued to be provided to any offeree or offeree representative who, during the course of the transaction, indicates that he is not interested in purchasing the securities offered, or, except in the case of any undertaking made pursuant to subparagraph (c)(3), to whom the issuer or any person acting on its behalf has determined not to sell the securities

(f) Business Combinations.

(1) The term "business combination" shall mean any transaction of the type specified in paragraph (a) of Rule 145 under the Act.

(2) All the conditions of this rule except paragraph (d) and subparagraph (h)(4) shall apply to business combinations.

NOTE: Notwithstanding the absence of a written agreement pursuant to subparagraph (h)(4), any securities acquired in an offering pursuant to paragraph (f) are restricted and may not be resold without registration under the Act or an exemption therefrom.

(3) For purposes of paragraph (f) only, the issuer and any person acting on its behalf after making reasonable inquiry, shall have reasonable grounds to believe, and shall believe, at the time that any plan for a business combination is submitted to security holders for their approval, that each offeree either alone or with his offeree representative(s) has such knowledge and experience in financial and business matters that he is or they are capable of evaluating the merits and risks of the prospective investment.

(4) In addition to information required by paragraph (e), the issuer shall provide, in writing, to each offeree at the time the plan is submitted to security holders for approval, information about any terms or arrangements of the proposed transaction relating to any security holder that are not identical to those relating to all other security holders.

(g) Number of Purchasers.

(1) There shall be no more than thirty-five purchasers of the securities of the issuer from the issuer in any offering pursuant to the rule.

NOTE: See subparagraph (b)(1), the note thereto and the Preliminary Notes as to what may or may not constitute an offering pursuant to the rule.

(2) For purposes of computing the number of purchasers for subparagraph (g)(1) only:

(i) the following purchasers shall be excluded:

(a) any relative or spouse of a purchaser and any relative of such spouse, who has the same home as such purchaser; and

(b) any trust or estate in which a purchaser or any of the persons related to him as specified in subdivision (g)(2)(i)(a) or (c) collectively have 100 percent of the beneficial interest (excluding contingent interests);

(c) any corporation or other organization of which a purchaser or any of the persons related to him as specified in subdivision (g)(2)(i)(a) or (b) collectively are the beneficial owners of all the equity securities (excluding directors' qualifying shares) or equity interest; and

(d) any person who purchases or agrees in writing to purchase for cash in a single payment or installments, securities of the issuer in the aggregate amount of $150,000 or more.

NOTE: The issuer would have to satisfy all the other provisions of the rule with respect to the purchasers specified in subdivision (g)(2)(i).

(ii) There shall be counted as one purchaser any corporation, partnership, association, joint stock company, trust or unincorporated organization, except that if such entity was organized for the specific purpose of acquiring the securities offered, each beneficial owner of equity interests or equity securities in such entity shall count as a separate purchaser.

NOTE: See Preliminary Note 5 as to other persons who are considered to be purchasers.

(h) Limitations on Disposition. The issuer and any person acting on its behalf shall exercise reasonable care to assure that the purchasers of the securities in the offering are not underwriters within the meaning of Section 2(11) of the Act. Such reasonable care shall include, but not necessarily be limited to, the following:

(1) making reasonable inquiry to determine if the purchaser is acquiring the securities for his own account or on behalf of other persons;

(2) placing a legend on the certificate or other document evidencing the securities stating that the securities have not been registered under the Act and setting forth or referring to the restrictions on transferability and sale of the securities;

(3) issuing stop transfer instructions to the issuer's transfer agent, if any, with respect to the securities, or, if the issuer transfers its own securities, making a notation in the appropriate records of the issuer; and

(4) obtaining from the purchaser a signed written agreement that the securities will not be sold without registration under the Act or exemption therefrom.

NOTE: Subparagraph (h)(4) does not apply to business combinations as described in paragraph (f). Notwithstanding the absence of a written agreement, the securities are restricted and may not be resold without registration under the Act or an exemption therefrom. The issuer for its own protection should consider, however, obtaining such written agreement even in business combinations.

Four confidential engagements concerning the valuation of capital stock.

Valuations of a business enterprise involving extensive market investigations of capital stock prices.

Champion International	The Stanley Works
Mobil Chemical Co.	Stone Container Corp.
Handy & Harman	Veeder Industries
Bundy Corporation	Gould, Inc.

Other engagements relating to consultation service in the areas of taxation, accounting, and rate-making.

Questor Corp.	Pennwalt Corp.
Quaker Oats Co.	American Can Company
NL Industries	Warnaco

Purpose - The purpose of this appraisal is to develop and express an opinion of the fair market value of 77,160 Class B common shares of Modern Maid Food Products, Inc. as of August 21, and September 24, 1968 for gift tax purposes. More specifically, the ownership of the shares being appraised is divided as follows:

Given in trust August 21, 1968 for the benefit of:		
Stanley Silverman	25,680	shares
Joel Silverman	25,680	shares
Given in trust September 24, 1968 for the benefit of:		
Susan Silverman	8,600	shares
Ann Silverman	8,600	shares
Beth Silverman	8,600	shares
Total	77,160	shares

The term "fair market value" as used herein is defined as the amount at which the assets would exchange between a willing buyer and a willing seller, neither being under compulsion, each having reasonable knowledge of all relevant facts, and with equity to both.

Background - Modern Maid Food Products, Inc. was formed as a New York Corporation in 1952 as the successor to a partnership formed in 1933. The company has two wholly-owned subsidiaries, Modern Maid Food Products of Louisiana, Inc., and

Modern Maid Realty Corp., both incorporated under the laws of the State of Louisiana. The company manufactures breading and batter mixes, prepared to customers' specifications. The company also manufactures prepared flour mixes for use in restaurants, hotels, and other institutional outlets. The offices of the company are located in Garden City, New York.

On August 12, 1968, the company exchanged newly authorized Class A and Class B common stock and shares of 5% cumulative preferred stock for the then outstanding common stock. The resulting capitalization was as follows:

Class A Common Stock	21,600 shares
Class B Common Stock	86,400 shares
Cumulative Preferred Stock, 5%	25,200 shares

The Class A and Class B common stock rights were identical except that all voting rights were vested in the Class A common stock.

On August 21, 1968, Mr. Jack Silverman, Chief Executive Officer of the company and holder of the majority interest in the Class A common stock, gave in trust 25,680 Class B common shares to his son, Stanley Silverman and 25,680 Class B common shares to his son, Joel Silverman. Shortly thereafter, on September 24, 1968, Seymour Silverman established three trusts for his daughters, Susan, Ann and Beth, giving 8,600 shares of Class B common stock to

each trust. The subject valuation concerns the fair market value of these various stock interests as of the respective dates of transfer.

As part of this appraisal, I held discussions with company management to gain a familiarity with the nature and operations of the business. In addition, financial statements audited by Arthur Andersen & Co. were provided to me and have been accepted without investigation as properly reflecting business operations. These income statements for the years 1964 through 1967 and the balance sheet as of December 31, 1967 have been reproduced in this report and appear as Exhibits 1 and 2, attached.

Valuation - In any valuation of property, consideration must be given to the values indicated by the cost to replace the property, the income-producing capabilities of the property, and the price paid for comparable property in an active, public market. With respect to shares of capital stock, the valuation approach based on market value is considered to be the most appropriate.

In the course of this study, consideration has been given to the following:

1. the history of Modern Maid Products, Inc. and the nature of its business.
2. the financial condition of Modern Maid, the nature of its assets, and the book value of the stockholders' equity.
3. the historical operating results of Modern Maid.
4. the investors' appraisal of the common stock of companies in similar lines of business as evidenced by the ratio of earnings to the price of their common shares, where it is publicly traded.
5. the general economic and stock market conditions at and around August, 1968.
6. such other factors as have a bearing on the fair market value of the shares.

Where an appraisal is made of the capital shares of corporations which are publicly traded in the stock market, the valuation procedure is rather straightforward. The value, in this case, is represented in most instances by the known amount at which the shares would sell in the public market, net of selling costs and taxes. With respect to the capital

shares of Modern Maid which are being appraised, the procedure is made considerably more difficult due to the fact that the shares are closely held. The only sale of these shares was that of 4,790 shares to 19 persons in August, 1968 at a price of $10.00 per share.

In addition, the capital shares of Modern Maid are "restricted" securities that can not be distributed publicly without registration under the Securities Act of 1933. Such securities can only be acquired directly from the issuing corporation in a private placement, or from an existing holder. In either case, however, the transaction is privately negotiated and carries with it a "letter" contract to the effect that the security is being purchased as an investment and will not be re-offered for sale after a short period of time. Further, the number of buyers of a restricted security is limited to avoid being construed as a public offering, which would require registration with the Securities and Exchange Commission.

Valuation Premise - The valuation of the designated Class B common shares of Modern Maid is based on comparative analysis of prices of the capital stock of publicly traded companies in a similar business, modified by the limiting conditions,

under which these shares could be sold. These conditions arise due to the following facts:

1. Modern Maid Products, Inc. capital stock is not publicly traded.
2. The marketability of these shares is further restricted in that: (a) the prospective purchasers must be relatively few in number requiring a substantial individual investment, (b) a prospective purchaser must be willing to hold them as a long term investment with no guarantee of a future public market, (c) these shares carry no voting rights and (d) the control of the issuing corporation is in the hands of a single individual.

Valuation Technique - As a first step in the valuation an investigation was made into the economic conditions and the general atmosphere of the securities market in August-September, 1968. During 1968, the stock market, as evidenced by the Standard & Poors index, moved upward, reaching an all-time high for that time, of 108.31 (1941-1943 equals 10) in the second quarter of 1968. The price earnings ratio of

Standard & Poors index of 425 industrial stocks was 17.39 during the second quarter of 1968. In mid-August of 1968, the price earnings ratio of the Dow Jones Industrial stocks was 15.9. The price earnings ratio of Barron's 50 stocks at this time was 15.4. In mid-September, these price earnings ratios were 16.8 and 16.3, respectively. While there were forecasts of some slowdown in the economy, the general atmosphere of the securities market was generally favorably at this time.

I concluded as a result of this investigation that there was no appreciable difference in the market climate between the dates of August 21, 1968 and September 24, 1968 to warrant their separate consideration for purposes of this valuation.

Specifically, a search was made for companies in a similar business to Modern Maid and whose securities were publicly traded. The following were selected as being the most closely representative of this group:

American Bakeries Co.
Continental Baking Co.
Interstate Bakeries Corp.
General Foods Corp.
Pillsbury Co.
Quaker Oats Co.

It is recognized that these firms are very large, and enjoy diversified markets, and that these facts must be considered in any comparison with Modern Maid. The relative sizes and price to earnings ratios of these companies are as follows:

	1967 Net Sales (000,000's)	August 1968 Price/Earnings Ratio
General Foods Corp.	1,652	18
Continental Baking Co.	621	16
Quaker Oats Co.	555	19
Pillsbury Co.	526	18
American Bakeries Co.	298	13
Interstate Bakeries Co.	196	12

The net sales of Modern Maid in 1967 were $11.7 million, having grown at the rate of 6.5% during the previous three years. Further, with regard to Modern Maid, the following data was developed as of December 31, 1967:

Debt/Equity ratio	0.3
Current ratio	2.9
Quick ratio	2.6
Sales/Working capital	4.7
Sales/Accts. Receivable	4.4

This data indicates, in my opinion, that would exhibit, to a potential investor, adequate financial resources for the future growth of its business.

In determining the value of the Modern Maid equity if it were publicly traded, I have given consideration to:

1. The price/earnings ratios of the firms shown above.
2. Modern Maid's relative small size.
3. The fact that Modern Maid was a regional, non-diversified company.

I have, therefore, concluded that the equity of Modern Maid, if offered to the public market would sell at a price/earnings ratio of 10. This includes a consideration that shares of unknown companies offered to the public are often "underpriced" in order to make them attractive to the buying public and to help assure a strong after-issue market.

For Modern Maid, the earnings to which this multiple should be applied must be determined. It assumed that a potential investor in Modern Maid's securities at August 1968 would have available to him the income statements for 1964 through 1967 which have been reproduced as Exhibit 1 of this report. While the net sales of

Modern Maid for the period 1964 through 1967 exhibited a steady growth, the net income presented an unsteady pattern. For this reason, I considered it appropriate to average the income for the three years prior to the valuation:

	Net Income (ooo's)
1965	$ 622
1966	589
1967	636
Average	$ 616

On the basis of average earnings of $616,000 multiplied by the price earnings ratio of 10, it is estimated that the fair market value of the equity of Modern Maid Products, Inc. as of August 1968 was $6,160,000, assuming the securities were being traded in an active, public market.

Since these securities were not, in fact, publicly traded, an adjustment must be made for this to recognize the lack of liquidity inherent in the purchase of closely held securities.

One measure of this adjustment which has been utilized is the costs incurred by companies in offering their capital

stock to the public market. These costs include underwriting fees, commissions, legal and consulting fees, and management expenses. I have concluded that a discount of 15% would be an appropriate adjustment.

Applying this adjustment to the publicly traded value of $6,160,000 yields an adjusted value of $5,236,000. This represents the fair market value of the equity of Modern Maid with consideration of its closely held status.

As previously noted, the equity of Modern Maid Products, Inc. consisted of both preferred and common stock. The preferred stock was comprised of 25,200 shares of cumulative $100.00 par value stock with a 5% dividend. The total dividend requirement on an annual basis for these shares of preferred stock was $126,000. Considering the net income available in the previous three years, the payment of this dividend is relatively secured and the cumulative feature further protects the investor in these securities.

I then made an analysis of publicly traded issues of cumulative preferred stock with a Standard & Poors rating of BBB or BB. These issues were considered to be comparable

with the Modern Maid preferred shares if it were publicly traded and subject to such a rating. Nine such issues were analyzed and the average yield of the group was 6.4%. I have, therefore, concluded that investors in preferred stock of comparable quality to that of Modern Maid desired this level of return on their investment. Therefore, in order to obtain this level of yield, the price which would be paid would be correspondingly less than the par value and is measured by the capitalization of the stated dividend ($5.00) at the investor's rate of 6.4%, or $5.00 ÷ .064 = $78.13. I have used $80 per share, considering Modern Maid's dividend coverage of 5 times. On this basis, the indicated value of the 25,200 shares of Modern Maid preferred stock is $2,016,000.

If $5,236,000 represents the fair market value of the equity of Modern Maid, then this amount, less $2,016,000 represented by the preferred shares, or $3,220,000, remains at the value of the common shares.

The total issued and outstanding common shares of Modern Maid at August 1968 were as follows:

Class A Common	21,600	shares
Class B Common	84,400	shares
Total	108,000	shares

On a per share basis, the fair market value attributed to the common shares of $3,220,000 is $29.81.

This value of $29.81 per common share represents, in my opinion, the fair market value of the Modern Maid common shares if an investor could purchase a minority interest in one clas of common stock with the typical rights with respect to voting, dividends, and capital distribution.

As we have pointed out, this is not a possibility with respect to the shares being appraised and a further adjustment must be made.

A further consideration must be made at this point of the lack of marketability of the Class B common shares being appraised due to the fact that they represent a separate class of common shares, do not have any rights for future registration, and do not carry with them the voting power to compel a future registration. As a measure of the loss of marketability due to this condition, an analysis was made

of the purchases of such securities by the Value Line Development Capital Corporation during the period of January 1 to July 23, 1968. This investment company makes a speciality of the purchase of restricted securities.

During 1968, four such investment companies were formed:

The Diebold Technology Venture Fund, Inc.
Fund of Letters, Inc.
SMC Investment Corporation
The Value Line Development Capital Corporation

Of these, only Value Line was in existence long enough to have recorded experience by August 1968.

The Value Line analysis compares the price paid for restricted securities compared with the average market price of the "free" (registered) securities of the same corporations. The data included in this study is presented as Exhibit 3, attached.

This data indicates that the purchase price of the restricted securities represented a discount ranging from a low of 16.7% to a high of 71.4% when compared with the average market price of the free securities on the date of acquisition. The average discount was 44%. A further examination indicates that one half of the securities analyzed showed discounts over 40% and that their average was 57.2%.

The reason for the discount which is exhibited in this analysis has been well stated in the following excerpts from the February 1, 1968 prospectus of the Value Line Development Capital Corporation:

> "In many cases there will, after the corporation's initial operating period, be no public market for the portfolio securities of the corporation representing investments in development situations. Accordingly, it may be difficult to sell such securities at a price representing, in the opinion of management, their fair value until such time as the issuers of such portfolio securities have developed to the point where such securities are treated in a public market."
>
> "Where registration is required, a considerable period may elapse between the time when a decision is made to sell the securities and the time when the corporation would be permitted to sell under an effective registration statement. During such period, if adverse market conditions develop, the corporation may not be able to obtain as favorable a price as that prevailing at the time of the decision to sell."

The prospectus of the Diebold Technology Venture Fund, Inc. issued July 12, 1968 states similarly:

> "As previously indicated, it is expected that a substantial portion of the funds' portfolio may consist of highly speculative securities with no public market or a limited public market, issued by small and unseasoned companies..... In many cases, it may take several years before portfolio securities of unseasoned companies are considered to have become sufficiently valuable and appropriate for sale. It is expected

> that a substantial portion of these securities may be purchased by the fund subject to investment representations or under other circumstances which would require registration of the securities under the Securities Act of 1933 in connection with a subsequent public sale. Such a registration may result in material delays in making a sale as well as exposure to a loss from a declining market."

In these statements, these knowledgeable investors set forth the risks which are inherent in the purchase of restricted securities of unseasoned companies, of which the Class B shares of Modern Maid are an example.

Further, after recognizing that these risks exist, these investment companies have sought to reduce this risk in a number of ways. Value Line has stated that it is a policy that at least 50% of the value of restricted securities in its portfolio must be the subject of a commitment from the issuer to register, at Value Line's request, the securities under the Securities Act of 1933. That is, the restricted securities are bought with a registration agreement as a condition of the purchase. Similarly, SMC Investment Corp. entirely limits its purchase of restricted securities to those corporations where there already exists some free stock in the public market. The Fund of Letters, Inc. states that its portfolio is mostly of restricted stocks of corporations which also have free stocks in the market. These policies of

the funds reduce the amount of risk in two ways. First, where the fund owns restricted securities of a corporation which has publicly traded shares, the fund has access to financial data on the corporation and the value of the publicly traded shares serves as a benchmark to indicate the public investor's appraisal of the company. Secondly, by providing as a condition to the purchase of restricted securities an agreement for future registration, the funds are assured that if growth in the issuing corporation takes place as expected, a public market for their shares can be utilized.

Any analysis of the discounts set forth above, then, must give consideration to the fact that they exist after consideration of the efforts of the fund to reduce the risk as discussed. With respect to the Class B common shares of Modern Maid being appraised, a prospective purchaser of these securities has absolutely no assurance that the securities would ever be subject to registration in the future, and must consider that the control over a decision to register any securities of Modern Maid rests with a single majority stockholder.

Further, since there were no publicly traded shares in existence, such an investor would likely not be able to obtain any financial and operating data on the company whose shares he owned.

A potential investor in these shares, therefore, would, in my opinion, have to be willing to invest a substantial amount (due to the restrictions on the number of possible buyers) at a greater risk of being able to capitalize on the expected growth of Modern Maid than that taken by the investment companies cited above.

After careful consideration of these facts, it is my opinion that an appropriate discount to be applied to the Class B common shares of Modern Maid Products being appraised is 60%. Applying this discount to the previously determined price per share of $29.81 yields a price per share of $11.92.

Conclusion - After consideration of the facts outlined above, and the employment of valuation techniques which, in my practical experience I consider appropriate, it is my conclusion that the fair market value of the 77,160 Class B common shares of Modern Maid Food Products, Inc. as of August 21 and September 24, 1968 is fairly stated in the amount of $12.00 per share.

Exhibit # 1

MODERN MAID FOOD PRODUCTS, INC.

and Subsidiary Corporations

Consolidated Statement of Operations

(000's)

	1964	1965	1966	1967
Net Sales	8,256	9,772	10,674	11,739
Cost of Sales	5,291	6,292	7,163	7,710
Gross profit	2,965	3,480	3,511	4,029
Selling, G & A expense	2,105	2,300	2,413	2,789
Operating income	860	1,180	1,098	1,241
Other Income (expense)	(3)	15	30	43
Income before taxes	856	1,195	1,127	1,284
Taxes	430	573	538	649
Net Income	426	622	589	636

(may not add due to rounding)

MODERN MAID FOOD PRODUCTS, INC.

and Subsidiary Corporations

Consolidated Balance Sheet
December 31, 1967

(000's)

ASSETS

Current Assets		
Cash	498	
Acc'ts. Receivable	2,656	
Inventories	415	
Cert. of Deposit	150	
Interest Rec.	4	
Total Current Assets		3,724
Fixed Assets		
At Cost	2,314	
Depr. Reserve	1,039	
Net Fixed Assets		1,275
Other Assets		
Deposits	54	
Investments	26	
Cash Value-Ins.	33	
Deferred Charges	13	
Net Leasehold	4	
Total Other Assets		130
TOTAL ASSETS		5,128

LIABILITIES AND CAPITAL

Current Liabilities	$	
Accts. Payable	744	
Taxes Withheld	25	
Accrued Expenses	238	
Fed. Income Taxes	212	
Due to Officers	22	
Notes Payable	36	
Total Current Liabilities		1,277
Capital		
Common Stock	216	
Preferred Stock	144	
Surplus	3,491	
Total Capital		3,851
TOTAL LIABILITIES		5,128

(may not add due to rounding)

THE VALUE LINE DEVELOPMENT CAPITAL CORPORATION

PURCHASES OF RESTRICTED SECURITIES

January 1 - July 23, 1968

	Acquisition Date	# Shares	Cost Per Share	Average Market Price-Free Stock	Indicated Discount
Aerological Research, Inc.	5/10/68	35,000	$ 7.00	$ 12.38	43.5 %
Clayton Corp.	7/24/68	100,000	5.25	7.81	32.8
E. L. I. Industries, Inc.	7/1/68	30,000	9.70	19.00	48.9
Jayark Corp.	4/24/68	45,450	5.50	16.25	66.2
Landa Industries, Inc.	6/10/68	75,000	3.33	7.50	55.6
Metalurgical Int'l. Inc.	4/4/68	20,000	25.00	33.00	24.2
Miles-Samuelson, Inc.	5/29/68	45,000	7.25	11.50	37.0
Process Plants, Inc.	7/23/68	25,000	30.00	50.00	40.0
Tally Corp.	5/21/68	10,000	30.00	45.25	33.7
Tintair, Inc.	4/5/68	250,000	1.00	2.38	58.0
United Utilities - Florida	7/16/68	20,000	2.50	8.75	71.4
The Valtronic Corp.	3/11/68	50,000	5.00	6.00	16.7

Exhibit #3

Ex 19

APPRAISAL

MODERN MAID FOOD PRODUCTS, INC.

CLASS "B" COMMON STOCK

HERBERT S. CANNON

111 Broadway

New York, N.Y. 10006

Philips, Appel & Walden, Inc.
Member New York, American and Other Principal Stock Exchanges

111 BROADWAY · NEW YORK, NEW YORK 10006
CABLE ADDRESS - BROKERAGE
TELEX - 62206

TELEPHONE
(212) 964-9000

BRANCH OFFICES
FORT LEE, NEW JERSEY
VIENNA, AUSTRIA

March 22, 1974

Mr. Sidney Gelfand
136 East 57th Street
New York, New York

Dear Mr. Gelfand:

Pursuant to your request, I have made a study of the financial and market factors affecting the fair market value of 51,360 shares of Class B (non-voting) Common Stock of Modern Maid Food Products, Inc. on August 21, 1968 and the fair market value of 25,800 shares of said stock on September [illegible] 1968.

The appraisal report details the following data:

(a) My qualifications as an appraiser of securities for market values.

(b) Nature of the stock and relevant statistical data.

(c) Valuation factors.

In my opinion, the fair market value of the Class B Common Stock of Modern Maid Food Products, Inc., subject to gifts on August 21, 1968 and September 24, 1968, was not in excess of $2.00 to $5.00 a share dependent upon the anticipated time the company would remain privately owned.

Sincerely,

Herbert S. Cannon
President

HSC/lb
enclosure

QUALIFICATIONS - HERBERT S. CANNON

EDUCATION

1949	Cheshire Academy, Cheshire, Connecticut	
1953	Washington and Jefferson College	B.A.
1960	Fordham Law School	LL.B.
1968	Fordham Law School	J.D.
1969	Admitted to the Supreme Court of the United States	

BUSINESS HISTORY

1962 - 1970	Weis, Voisin, Cannon & Co., Inc. and predecessor firms (Members of the New York Stock Exchange)	President and Director
1967 - 1970	Elgin National Industries, Inc. (Listed on the New York Stock Exchange)	Chairman of the Board
1971 - 1973	Cannon, Jerold & Co., Inc. (Members of the New York Stock Exchange)	Chairman of the Board and President
1970 to present	Cannon Industries, Inc.	Chairman of the Board
1971 to present	Solvent Chemical Company, Inc.	Chairman of the Board
1973 to present	Philips, Appel & Walden, Inc. (Members of the New York Stock Exchange)	President and Director

PAST DIRECTORSHIPS

The Franklin Mint	Listed on the American Stock Exchange
Bartell Media Corporation	" " " " " "
Thompson-Starrett Corp.	" " " " " "
Diversified Data Services & Sciences, Inc.	" over-the-counter
Product Applications, Inc.	" " " "
Carson Chemical Corporation	Private corporation
Data Information Services, Inc.	Listed over-the-counter
Generics Corporation of America	" " " "

CURRENT DIRECTORSHIPS AND CONSULTING ASSOCIATIONS

Decision Systems, Inc.
Electro-Catheter Corporation
Nation-Wide Check Corporation

Financial Consultant to several public corporations (Past and Current):

Bartell Media Corporation (ASE)
Briggs Leasing Corporation (OTC)
Diversified Data Services & Sciences, Inc. (OTC)
Electro-Catheter Corporation (OTC)
Elgin National Industries, Inc. (NYSE)
The Franklin Mint (ASE)
Generics Corporation of America (OTC)
Romanoff Industries, Inc. (OTC)
Royal Zenith Corporation (OTC)
Solvent Chemical Company, Inc. (Private)
Thompson-Starrett Corporation (ASE)
The Tower Fund, Inc. (OTC)
Ultimacc Systems, Inc. (OTC)

BUSINESS EXPERIENCE

I have been in charge of several finance committees of charitable organizations including the raising of capital, interim capital investment and the evaluation of operating costs and expenses.

I have served on the investment committee of The Tower Fund, Inc. which invested approximately $6,000,000.

I am a trustee of Washington and Jefferson College and a member of its finance committee which invests approximately $25,000,000.

During 1956 - 1960 I acted as an investment analyst in the evaluation of corporations for investment, merger or acquisition.

I have often served as an appraiser in the sale and merger of several public and private corporations (e.g., Rayne Industries, Incorporated, Butler Capital Corporation, Generics Corporation of America, Nation-Wide Check Corporation, Haber & Henry, Inc.) I have acted as financial consultant to Field's Baking Corporation (manufacturers of bread and bread crumbs) and to the Pechter-Field's Baking Corporation merger.

During 1962 - 1970, as President of Weis, Voisin, Cannon & Co., Inc., I was totally responsible for all financial involvements of the corporation including its syndications, negotiation of underwritings, the financial consulting department, and the corporate finance department which was instrumental in effecting a number of mergers, acquisitions and dispositions in 1967, 1968 and 1969 to the extent of:

Nature of Service	Number	Dollar Volume
Private Placements	15	$ 15,000,000
Underwritings, as Manager		100,000,000
Underwritings, as Participant		200,000,000
Mergers and/or Acquisitions		15,000,000

In 1967 I negotiated for control of the Thompson-Starrett Corporation (ASE) and became Chairman of the Board. In the three ensuing years I was instrumental in making nine acquisitions, all of which required financial evaluations of both public and private entities.

I have qualified as an expert witness in approximately seven arbitration and court proceedings requiring the evaluation of corporate worth.

NATURE OF THE STOCK AND RELEVANT STATISTICAL DATA

1. Modern Maid Food Products, Inc. was a privately owned corporation in 1968 having but three principal stockholders, one of whom owned more than 50% of the company. It was engaged in the business of manufacturing breadings and batter mixes and prepared flour mixes for sale to industrial and large commercial purchasers.

2. The Class B Common Stock of Modern Maid Food Products, Inc. was non-voting stock by the corporation's very charter and there were 86,400 shares outstanding.

3. The voting control of the corporation was lodged in the 21,600 shares of Class A Common Stock outstanding of which 12,840 shares were owned by one individual only sixty years of age.

4. Preceding the common stock were 25,200 shares of 5% cumulative preferred shares with a par value of $100 per share.

5. The book value of a common share of Modern Maid Food Products, Inc. (consolidated basis) at December 31, 1967 was $12.31 a share. Projecting 1967's earnings to August 31, 1968 on a time basis would give a book value of $15.98 a share after preferred dividends.

6. Average yearly earnings before dividend requirements in 1965, 1966 and 1967 were $615,789 and $489,789 after giving effect to the preferred dividend requirements after the recapitalization on August 12, 1968. This latter amount would be $4.53 per share on the 108,000 common shares outstanding.

7. No dividends were being paid on the common stock in 1968. Dividends paid in prior years were materially less than the preferred dividend requirements after the reorganization.

VALUATION FACTORS

1. Fair Market value is defined as the price a seller could obtain from a willing buyer having knowledge of all of the facts.

2. Modern Maid Food Products, Inc. was a privately owned corporation.

3. The Class B Common Stock was non-voting without any say in the management or control over business operations.

4. The Class B Common Stock had no marketability or immediate potential for same.

5. The type of business engaged in and the earnings multiple it might enjoy as a public vehicle.

6. The relative little growth in net earnings in the three years ended December 31, 1967 while sales increased 15%.

7. The amount of money that might be required to effect a purchase of 25,680 shares or 51,360 shares on August 21, 1968 and 8,600 shares or 25,800 shares on September 24, 1968, thus limiting the potential market.

APPROACHES

(a) A Conservative Investor may be ruled out due to the lack of liquidity, lack of dividend and the inability to have a say in management, planning, financial policies or in the possible sale or liquidation of the business.

(b) A Speculator! Due to the non-voting features of the stock and lack of market, the relative young age of management owners, the lack of incentive by management to declare dividends on the common stock (even if the corporation could afford such action), such an investor would only be interested in the possibility of a public offering some time in the future. Without a voice in management, he would be dependent upon the desires and whims of management in this respect.

A person taking such a speculative position requiring a substantial sum of money anticipates a market price profit of at least 400% within a three year period. Even if a public offering is effected, an insider's stock is usually restricted for an additional period of years from public sale.

Although underwriting conditions were good in August and September 1968, the nature of the company's business and the relative flatness of earnings in 1965, 1966 and 1967 (deviation from the mean being about 3% on the upside and 6% on the downside), this would limit the value to be placed on the company as a whole to ten times average earnings or $6,158,000. Deducting preferred stock of $2,520,000 gives a common stock potential market value of $3,638,000 or $33.70 a share if public. Since speculative investments in non-marketable closely held situations are made on the basis of a 400% paper profit, within three years, the most such an investor would pay is 20% of $33.70 or $6.75 a share. Such a price would require an investment of $173,340 from two purchasers of 25,680 shares each and $58,000 from three additional purchasers of 8,600 shares each. It would be extremely difficult to find five speculative investors with such available funds, willing to take the risk of being hung up with non-voting stock in a privately owned company with no return on investment. If only one individual were available, for such a purchase an amount in excess of $500,000 would be required, again diminishing the availability of buyers and reducing the fair market value to approximately $5.00 per share.

If a public offering or merger with a public entity could not be reasonably expected within a three year period, then I would be loathe to invest or advise any one to invest at more than a nominal amount of $2.00 per share. The amount to be invested at $5.00 a share, possibly as much as $385,000 is too significant an amount to wait upon a pure conjecture without a real possibility of liquidating one's investment.

What must be emphasized here is the purchaser of the Class B Common Stock (non-voting) without the ability to force management to change the status of the stock from non-voting common to voting common could entertain no probability of ever liquidating the stock in the public market. Due

to different class status, none of the rules of the S.E.C. or NASD permit an automatic registration, even after a substantial holding period, to enable even piece meal liquidation into the public market. This factor alone would greatly depreciate the fair market value of the stock by 70% even where underwritings are being considered.

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STOCK VALUATION

MODERN MAID PRODUCTS, INC.

1968

ESTABLISHED 1899

THE MANUFACTURERS' APPRAISAL COMPANY

Atlanta
Boston
Baltimore
Chicago
Cincinnati

Executive Offices
ROBINSON BUILDING
15th & CHESTNUT STREETS
PHILADELPHIA, PA. 19102

Cleveland
Detroit
New York
Philadelphia
St. Louis

Philadelphia, Pa.
March 14, 1974

Internal Revenue Service, Regional Counsel
26 Federal Plaza,
New York, New York 10007

Gentlemen:-

We are pleased to submit our appraisal of certain Class B Common Stock of Modern Maid Products, Inc.. It is our considered opinion that the Fair Market Value of the Stock, constituting a minority interest and as of various dates in August, September and December 1968, is best expressed as $25 per share.

Our engagement has been confined to a determination of the value of the Stock in accordance with our agreement. We have not investigated title to the property, nor the possible existence of liens, mortgages and assessments and, therefore, do not assume responsibility with respect to ownership.

Neither the employment to make, nor the compensation for the appraisal is contingent upon values reported. To the best of our knowledge or belief, all statements and information contained in this report are true and correct, and no important facts have knowingly been withheld. The Manufacturers' Appraisal Company has no present, prospective, direct or indirect interest in the property herein appraised.

This analysis was made by the use of methods and procedures conforming to ethical standards of practice.

Respectfully submitted,

THE MANUFACTURERS' APPRAISAL COMPANY,

Vice President.

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PURPOSE OF APPRAISAL

The purpose of this appraisal is to estimate the Fair Market Value of certain Class B Common Stock of Modern Maid Products, Inc. as of various dates in August, September and December, 1968. The concluded values will consider the fact that the subject shares constituted only a minority interest in the subject company, that the stock was non-voting, and that there was no ready market for it.

DEFINITION OF FAIR MARKET VALUE

Fair Market Value is defined as the price expressed in terms of money which the subject stock will bring in a normal market, allowing a reasonable time to find a purchaser who buys with full knowledge of the subject company's advantages and disadvantages, with neither party being under compulsion to buy or sell.

The valuation of privately-held corporate stock, stock for which their is neither an established market price nor even a ready market, presents certain difficulties. Analysis of the subject stock poses several interesting valuation problems. First,the valuation dates are over five years in the past, making direct examination of the company's physical assets inappropriate, and necessitating analysis of data on an historical basis.

Second, the subject stock, although it represents an intrinsic share or part of Modern Maid Products, Inc., is both non-voting and a minority interest. Accordingly, once the total value of the subject company is determined, care must be taken to correctly apportion that total to the different classes of stock, with proper consideration of discounts in value for lack of marketability, lack of control, etc..

Third, there were few publicly-held companies which were truly comparable to the subject. Ultimately our comparisons included five companies which overlapped in some areas with Modern Maid Products, Inc., but which were dissimilar in other areas.

Fourth , one or more of the subsequent appraisal approaches to valuation must include some estimate of the future or "projected" profits of the company. The risks of reaching incorrect conclusions in these circumstances can be reduced if there is some historical basis for the expectations upon which the projections rest; and they may even be reduced considerably if quantitative historical data exists which points consistently to the same answers. If, for example a given historical progression of numbers was 70, 80, 90, 100 and 110, and the circumstances

surrounding the progression remains unchanged, it could be predicted with a degree of certitude that the most likely next number in the progression would be 120. In the case of the subject company, however, no such obvious progression exists, and the degree of certitude with which projections can be made is most certainly reduced from that of the first example. It is not however, reduced to the point of being unmeasurable, and if in fact it must be estimated in order to complete certain appraisal approaches, it can best be accomplished by a thorough examination of historical trends.

Finally, a number of appraisal techniques must be established which will provide an effective measure of the total value of the company. At the onset of this study a number of approaches to valuation were considered. Ultimately this number was reduced to three: 1 - Return on Net Worth Approach, 2 - Price-Earnings Ratio Approach, and 3 - Comparable Public Enterprise Approach.

VALUATION

RETURN ON NET WORTH APPROACH

This approach considers a normal return to the balance sheet net worth of the company. Excess return may be capitalized at a higher (intangible) rate of return and the resultant value added to the net worth to provide an indication of total company value. Inasmuch as the book net worth figure is likely to be understated, this approach will generally produce a lower limit of value. Examine the following summary:

Net Worth (12/31/67)	$3,921,320
Normal Return (At 13%)	509,772
Actual Return	620,406
Excess Return	$110,634
Capitalized at 15%	$737,600
Total Indicated Value (Rounded)	$4,658,920 $4,659,000

Company	Net Worth	Return	% Return
Martha White Foods, Inc.	$8,281,012	$1,451,583	17.53
Manischewitz (B) Co.	3,690,017	255,963	6.94
Bridgeford Foods Corp.	2,179,105	263,838	12.11
Sap's Foods, Inc.	1,150,343	181,227	15.75
Spaulding Bakeries, Inc.	2,798,349	339,180	12.12
Total/Composite	$18,098,826	$2,491,791	13.77%
Average	-	-	12.89%

Thus a rounded normal industry return of 13% is applied against the subject company's 12/31/67 book net worth of $3,921,320. The result, $509,772 is subtracted from the actual earnings of $620,406 to indicate those earnings related to assets, other than those included in net worth. Capitalizing the $110,634 on excess return at a 15% rate of return produces $737,600 in value to those assets other than those included in net worth, and a total value including net worth of $4,659,000 (rounded).

RETURN ON NET WORTH APPROACH--CONTD.

These figures are based upon financial information that was approximately nine months old at the time of the gifts of subject stock. Assuming in September 1968 some reasonable knowledge of current earnings, and net worth produces a considerably higher total value. Utilizing rounded earnings of $700,000 and net assets of $4,200,000($817,917.77 and $4,399,330.84 respectively were actually reported in 12/31/68 statements) produces the following indication of value:

Net Worth	$4,200,000
Normal Return (At 13%)	546,000
Actual Return	700,000
Excess Return	$154,000
Capitalized at 15%	1,026,667
Total Indicated Value	$5,226,667
(Rounded)	$5,200,000

Thus consideration of more current earnings and net worth information produces a total rounded indication of subject company value of:

$5,200,000

PRICE-EARNINGS RATIO APPROACH

This approach compares the earnings of the subject company to earnings of publicly-held enterprises having a determinable total value through the price of their stock. It was not possible to find companies which were completely comparable to the subject. However, those companies ultimately used for comparative purposes are similar in that they are involved in making and/or sale of baked products or convenience mixers and batters. Detailed information relating to these comparable companies is contained in the addenda to this report.

Examine the following summary:

Company	Total Value	Earnings	P.E. Ratio
Martha White Foods	$30,986,888	$1,451,583	21.3
Manischewitz (B) Co.	2,918,960	255,963	11.4
Bridgeford Foods Corp.	5,250,838	263,838	19.9
Sap's Foods, Inc.	2,052,288	181,227	11.3
Spaulding Bakeries Inc.	3,467,640	339,180	10.2
Totals/Composite	$44,676,614	$2,491,791	17.9
Average			14.8
Average w/o High and Low			14.2

Thus these five publicly-held enterprises indicate that a multiplier of 14 conservatively reflects the average relationship between earnings and price. Applying this to the subject company's earnings for the year ending December 31, 1967 ($620,406) produces a total value of $8,685,684.

This approach thus far has considered the use of publicly-owned companies whose securities possess good, or reasonably good,listed or quoted markets. The subject company's securities, on the other hand, are closely-held by a relatively few stockholders, and there is no listed or quoted

PRICE-EARNINGS RATIO APPROACH--CONTD.

market for them. The value of these securities has, so far, been determined just as if such a market existed. Adjustment thus should be made for this factor.

While the amount of this adjustment could perhaps, be determined on a "judgment" basis, it is our opinion that the most realistic method of measuring this negative element of value is to ascertain what the actual cost would be to create a public market for the securities. Since such a public market would normally be created by a public offering of the securities through investment bankers or brokers, the problem becomes one of determining the costs of such flotation.

Comprehensive data on the costs of public flotation of common stocks were compiled with respect to issues registered with it by Securities and Exchange Commission. This data is summarized as follows:

Size of Flotations (Millions of Dollars)	Number of Flotations	Cost of Flotation as a Percent of Gross Proceeds
Under - 0.5	4	19.69%
0.5 - 0.9	15	13.68%
1.0 - 1.9	25	12.48%
2.0 - 4.9	30	8.61%
5.0 - 9.9	9	6.38%
10.0 - 19.9	5	4.88%
20.0 - 49.9	2	5.48%

It will be seen that flotations have been grouped in accordance with the size of flotation. In the right-hand column is shown the cost of flotation expressed as a percentage of gross proceeds of the flotation to the company. It will be noted that, as the size of the flotation increases, the cost of flotation as a percentage of gross proceeds declines.

PRICE-EARNINGS RATIO APPROACH--CONTD.

Thus the cost of the subject flotation would be an estimated 6% - 8%. Utilizing 8% as a reasonable amount needed to make the subject stock truly marketable produces a rounded indication of total value of:

$7,990,000

COMPARABLE PUBLIC ENTERPRISE APPROACH

This approach is based upon the concept that the total value of the Subject Company may be ascertained through comparisons with similar public enterprises which, through the price of their stock, have a determinable total value.

Investors consider many factors in deciding what price to pay for a given stock. Three very important items are: earnings, net worth and sales; and comparisons between the comparable companies and the subject company on these basis will provide a meaningful approach to value. Ultimately five public companies were selected as the basis for comparison, and they are summarized in the addendum to this report. Examine the summary on the following page.

Thus the earnings, net worth and sales of the comparable companies are expressed as percentages of total value, averaged, and expressed as multipliers. Weighting the contributory importance of these factors to consider earnings most important and sales least important produces the following formula to value:

Value = 6.74 x earnings + .50 x net worth + .07 x sales.

Inserting the subject company data into the formula produces the following results:

Value = 6.74 x $700,000 + .50 x $4,000,000 + .07 x $13,000,000
= $4,718,000 + $2,000,000 + $910,000
= $7,628,000

Reducing this by the percentage (8%) needed to make this stock marketable, produces a total rounded value of:

$7,000,000

COMPARABLE PUBLIC

Year Ending	Company	No. of Common Shares	Average Price	Total Value
6/1/63	Martha White Foods, Inc.	1,101,756	28 1/8	$30,986,888
7/31/63	Manischewitz (B) Co.	53,072	55	2,918,960
11/1/63	Bridgeford Foods Corp.	600,101	8¾*	5,250,838
5/31/63	Sap's Foods, Inc.	256,536	8	2,052,288
12/28/63	Spaulding Bakeries, Inc.	420,320	8¼	3,467,640
	Total/Composite Data			$44,676,614
	Average Data			
	Indicated Average Multipliers			
	Weighted Equally (÷ 3)			
	Weighted (3-2-1)			
	Subject Data			
	Total			
	Less Discount for Lack of Marketability (At 3%)			
	Net Value (Rounded)			

*Offered 12/19/63

ENTERPRISE APPROACH

Earnings	Net Worth	Sales	Earnings As a % of Total Value	Net Worth As a % of Total Value	Sales As a % of Total Value
$1,451,583	$8,231,012	$40,000,353	4.68	26.73	129.29
255,963	3,600,017	9,786,494	3.77	126.40	335.25
263,838	2,179,105	10,000,474	5.02	41.50	192.16
181,227	1,150,343	5,431,515	5.83	56.05	264.66
330,160	2,798,349	10,004,022	9.73	80.70	314.46
$ 2,401,791	$18,008,826	$76,363,353	5.57	40.50	170.92
			7.42	66.20	247.16
			13.47	1.51	.40
			4.49	.50	.13
			6.74	.50	.07
			$700,000	$4,000,000	$13,000,000
			$4,718,000	$2,000,000	$910,000
					$7,628,000
					610,000
					$7,018,000
					$7,000,000

3143 x 1,600,000

CORRELATION AND CONCLUSION OF VALUE

Thus the approaches considered have provided the following indications of value:

Return on Net Worth	-	$5,200,000
Price-Earnings Ratio Approach	-	$7,990,000
Comparable Public Enterprise Approach	-	$7,000,000

Each of the three approaches possesses merit but none could be considered any more than a tool to the final Fair Market Value of all of the company's stock. Elements of value are contained in each of the methods used, but a conclusion of value can be made only after weighing the worth of each approach and using good sound judgment in the determination of final values.

The Capitalization of Excess Earnings on Net Worth offers evidence of total value. However, it is limited in that the data used is gathered compositely from different enterprises, each of which use different accounting principles and techniques, different rates of depreciation, etc., causing significant variation on expression of net worth. This approach tends also to express the understatement of fixed asset value as intangible value, which it is not, thereby producing minimal values.

The Price-Earnings Ratio Approach offers evidence of total value. It too has its limitations in that the data used is gathered compositely from different enterprises using different accounting techniques, different rates of depreciation, etc., causing variation on expression of earnings. Additionally, the total company value for the five comparable companies was developed by multiplying the total number of shares outstanding times the

CORRELATION AND CONCLUSION OF VALUE--CONTD.

average price per share for the year. If the stock were subject to large fluctuations in price, the results could be significantly distorted.

The Comparable Public Enterprise Approach also offers evidence of total value, and has the same limitations mentioned for the two preceding approaches. Since, however, it weights more than one factor, it is somewhat more likely to produce a reasonable estimate of value. Accordingly, it is our considered opinion that the total value of the subject company's stock is best estimated as $7,000,000.

Thus far we have considered only the total value of the subject company. We must still estimate the approximate per share value of the subject stock, which is a minority interest and Class B(non-voting). The capital stock outstanding as of the gift dates was as follows:

Class A Common Stock	-	21,600 Shares (par $10)
Class B Common Stock	-	91,190 Shares (par $10)
Preferred Stock	-	25,200 Shares (par $100)

The preferred stock was 5% cumulative non-voting stock, and redeemable at its $100 par value. Reducing the total value of the company by the value of the preferred stock ($2,520,000) provides an indication of $4,480,000 in value to all the common stock. Consideration of an equal value of all the shares of both Class A and Class B common stock(112,790) produces a per share value of approximately $40. Discounts for minority interests can vary from 10% to 50%. It is our considered opinion that 25% best reflects the proper discount to be applied to the value of the minority interest. A summary of court cases and a study of two-step acquisitions is presented within the Addendum of this report as substantiation for the discount. Application, of this 25% discount to the $40 per share value produces a value of the shares of stock of $30.

CORRELATION AND CONCLUSION OF VALUE--CONTD.

Whether or not the subject shares should be further reduced in value due to their being Class B(non-voting) is problematical. The element missing in non-voting stock is the same as is missing in a minority interest, namely - control. Inasmuch as we have already discounted the value of the to reflect a lack of control, it may be inappropriate to further reduce the value for the fact that it is non-voting. Nevertheless, in order to make some distinction between the two classes of stock, we feel that a further reduction in value of $5 per share is reasonable, and that the value of the subject shares of stock, being Class B (non-voting), constituting a minority interest is best expressed as:

$25 per Share

ADDENDUM

THE MANUFACTURERS' APPRAISAL COMPANY
Executive Offices
ROBINSON BUILDING
15th & CHESTNUT STS.
PHILADELPHIA, PA. 19102
215 568 – 6739

ESTABLISHED
1899

OFFICES IN
PRINCIPAL
CITIES

EX. 3.

APPRAISAL QUALIFICATIONS

of

Hugh A. MacMullan, III

Appraisal Experience:

(A) Currently employed as a Vice-President and field appraiser by The Manufacturers' Appraisal Company, a national organization founded in 1899. Initially employed to complete real estate valuations, making valuations of intangible assets including stock in closely-held corporations since 1968.

(B) Appraisal assistant to independent appraiser and real estate broker.

(C) Self-employed for three years in construction and renovation of residential and commercial real estate; with specific experience in preparing cost estimates and engineering breakdowns.

Formal Education:

(A) A.B. degree from University of Pennsylvania, 1961.

(B) Courses in the following:

(1) Urban Renewal - University of Pennsylvania.
(2) Real Estate Brokers and Salesmen - Delaware County Board of Realtors.
(3) Real Estate Analysis - Temple University School of Business.
(4) Real Estate Law - Temple University School of Business.
(5) Property Management - Temple University School of Business.
(6) Real Estate Valuation - Temple University School of Business.
(7) Real Estate Practice - Temple University School of Business.
(8) Real Estate Finance - Temple University School of Business.

Specific Qualifications:

(A) Qualified by written examination to use the designation of "Member, American Society of Appraisers", with listed specialty of intangible assets, including stock in closely-held corporations.

(B) Found qualified to present evidence in numerous courts, informal hearings, boards of review, arbitration sessions, etc..

Specific Qualifications--contd.

(C) Qualified for Real Estate Salesman's License by written examination in the Commonwealth of Pennsylvania.

(D) Prepared Fair Market Value appraisals for buyers or sellers of property where sale was contingent upon appraisal values.

(E) Prepared other Fair Market Value appraisals that were used and accepted by lending institutions for mortgage loan purposes.

(F) Qualified by written examination as an appraiser for the State of New York.

(G) Have appraised closely-held corporations, leasehold equities, good will, franchises, license agreements, covenants not to compete, patents, trademarks, copyrights, contracts, and other intangible assets.

(H) Made or participated in over 300 appraisals in 31 states. Some of the better known clients served include:

A O Industries
AMF Inc.
Addressograph Multigraph Corporation
The Anaconda Company
Milton Bradley
W. Atlee Burpee Co.
Capital Cities Broadcasting Co.
Falstaff Brewing Corp.
Hoechst Fibers, Inc.
INSILCO
The Internal Revenue Service
Keene Corporation
Lavino Shipping Co.
McGraw-Hill Co.
Mite Corp.
National Industries
PPG Industries, Inc.
Textron
Time-Life, Inc.
Triangle Industries

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COMPARABLE PUBLIC ENTERPRISE DATA

MARTHA WHITE FOODS, INC.

History: Incorporated in Tennessee May 31, 1946, name changed to Martha White Mills, Inc. in 1952, and to Martha White Inc. 1967, present title adopted September 26, 1967.

Business: Co. manufactures or processes and distributes convenience mixes, family flour, corn meal, baking mixes, edible dried beans and mixed feed in the southeastern U.S.. Co. also distributes convenience foods nation wide.

Consolidated Income Account, years ended:

	June 1,'68	June 3,'67
Net sales	$40,060,853	$38,290,379
Other Income	28,888	29,048
Total	40,089,741	38,319.427
Cost of sales	27,659,414	27,368,257
Selling, etc., exp.	8,930,137	7,701,837
Depreciation	460,442	451,465
Interest	66,073	98,564
Income Taxes	1,451,583	1,224,756
Net income	1,522,092	1,474,547
Prev. earn. surp.	5,434,366	4,198,539
Dividends (cash)	321,355	238,720
Earned surplus	(1)6,635,103	5,434,366
Earn. com. share	$1.38	(2)$2.01
No. of com. shares	1,101,756	(2)734,504

(1)$4,468,927 not restricted. (2)$1.34 on 1,101,756 shs. adj. for 3-for-2 stk. split 10/68

Consolidated Balance Sheet, as of:

Assets:	June 1,'68	June 3,'67
Cash	$1,521,554	$1,980,170
U.S. Treas. bills	1,242,032	... ...
Receivables	1,869,621	1,999,634
(2)Inventories	3,572,926	3,610,877
Prepayments	36,205	31,440
Total current	$8,242,338	$7,622,121
(1)Plant, eq., etc.	2,623,769	2,670,788
Land	102,452	102,452
Construction	271,675	2,088
Trademarks, etc.	19,005	19,005
Other assets	173,697	162,307
Total	$11,432,936	$10,578,761

MARTHA WHITE FOODS, INC.--CONTD.

Consolidated Balance Sheet--contd.

Liabilities:	June 1, '69	June 3, '67
Notes, etc., pay.	$121,000	$157,000
Accts. payable	717,532	689,112
Accruals	430,554	440,998
Income Taxes	782,838	990,375
Total current	$2,051,924	$2,277,485
Long term debt-	1,100,000	1,221,000
Common stk. ($1)	1,101,756	734,504
Capital surplus-	544,153	911,405
Earned surplus	6,635,103	5,434,367
Total	$11,432,936	$10,578,761
Net current assets	$6,190,414	$5,344,636
Net tang. com. sh.	$7.50	(3)$9.61

(2)Lower cost(fifo) or mkt. (3)$6.41 adj. for stk. split.

MANISCHEWITZ (B.) CO.

History: Incorporated in Ohio, May 15, 1914. Company founded in 1888

Business: Company makes matzos(un-leavened bread), matzo meal and farfel, cake meal, Tam Tam crackers, borscht, gefilte fish, baby foods and canned soups. It also distributes pickles, canned fruits, candies other kosher grocery items, including Kosher sacramental wine.

Consolidated Income Account, years ended July 31:

	1969	1968
Net Sales	$9,801,280	$9,786,494
Royalty income	409,656	357,934
Total	10,210,936	10,144,428
Cost of sales, etc.	7,705,232	7,760,347
Selling, etc., exp.	1,888,032	1,895,680
(1)Oper. profit	617,672	488,401
Oth. income, net	59,896	60,456
Total income	677,568	548,857
Interest	121,720	111,894
Income taxes	245,000	181,000
Extraord. charge	(3)50,000	... ...
Net income	260,848	255,963
Prev. earn. surp.	3,318,211	3,168,368
Common divs.	106,120	106,120
Earned surplus	(2)3,472,939	3,318,211
Earn. com. share	(4)$4.91	$4.82
No. of com. shares	53,072	53,072

(1)After $161,763(1968, $160,339) depr. & amort. (2)$385,000 not restricted. (3) Prov. for loss liquid. of inv. in & adv. to 50% owned Canad. Co, (4)$5.85 before extraord. charge.

Consolidated Balance Sheet, as of July 31:

Assets:	1969	1968
Cash	$399,289	$349,082
Short-term inv.	... ...	395,399
Receivables, net	1,591,041	1,128,566
(3)Inventories	1,787,537	1,706,834
Total current	$3,777,867	$3,579,381
(1)Net prop., etc.	1,352,856	1,233,033
Other assets	476,579	450,966
Intangibles	144,644	164,753
Deferred charges	75,578	78,567
Total	$5,827,524	$5,507,200

MANISCHEWITZ (B.) CO.--CONTD.

Consolidated Balance Sheet, as of July 31--contd.

Liabilities:	1969	1968
Accts., etc. pay.	$668,101	$495,822
Debt due	81,000	81,000
Income taxes	232,178	157,861
Total current	$981,279	$734,683
Long term debt	1,001,500	1,082,500
(2) Common stock	371,506	371,506
Donated surplus	300	300
Earned surplus	3,472,939	3,318,211
Total	$5,827,524	$5,507,200
Net current assets	$2,796,588	$2,845,198
Net tang. com. sh.	$69.72	$66.42
(1) Depr. & amort.	$1,790,476	$1,674,536

(2) 53,072 no par shs. (3)Lower cost or mkt.

BRIDGFORD FOODS CORP.

History: Incorporated in Calif. on Dec. 31, 1952.

Business: Business consists primarily of the manufacture and wholesale distribution of processed meats and other delicatessen foods. The sale of fresh, frozen and smoked meats and the manufacture and sale of frozen bread dough products and other miscellaneous items.

Consolidated Income Account, yrs. ended:

	Oct. 31,'69	Nov. 1,'68
Sales	$13,208,326	$10,090.474
Cost of Sales	10,603,073	7,987,345
Sell. etc. exp.	1,996,367	1,434,804
Depreciation	228,257	188,487
Fed. inc. tax	188,000	216,000
Net income	192,629	263,838
Prev. retain. earn.	482,302	313,982
Dividends	135,650	95,518
Retain. earn. 11-1	539,281	482,302
Earn. com. share	$0.28	$0.44
No. of com. shs.	704,301	600,101

Consolidated Balance Sheet, as of:

Assets:	Oct. 31,'69	Nov. 1,'68
Cash	$422,979	$180,400
Receivables	702,296	470,862
(2)Inventories	706,325	510,343
Prepayments	104,357	50,818
Total current	$1,935,957	$1,212,423
(1)Net property	1,479,150	1,026,146
Total	$3,415,107	$2,238,569
Liabilities:		
Accts. etc., pay.	$888,052	$646,008
Fed. inc. tax	70,396	165,717
Notes payable	50,000	... ...
Total current	$1,008,448	$811,725
Notes payable	121,554	... ...
Future inc. tax	106,000	78,000
Capital stk.($1)	704,301	600,101
Capital surplus	935,523	266,441
Retained earnings	539,281	482,302
Total	$3,415,107	$2,238,569
Net current assets	$927,509	$400,698
Net tang. com. sh.	$3.10	$2.24

SAP'S FOODS, INC.

History: Incorporated in Indiana June 1, 1955 as Sap's Bakery, Inc., succeeding to business founded in 1946. Present name adopted in March 1969.

Business: Engaged primarily in the production and sale of a variety of bakery products. Principal markets are supermarkets, institutions, restaurants and vending machine operators. In addition, Co. operates 3 restaurants through subsidiaries.

Consolidated Income Account, yrs. ended May 31(SEC report):

	1969	1968	1967
Net Sales	$6,762,266	$5,431,515	$4,760,539
Cost & exps.	6,127,184	4,967,943	4,395,998
Depr. & amort.	166,152	134,983	129,652
Interest	33,497	25,350	25,290
Inc. taxes	201,170	122,012	83,382
Minority int.	3,048	... ...	... ...
Net income	231,215	181,227	126,217
Earn., com. sh.	$0.90	$0.71	$0.49

On 256,538 shs. outstg.

Consolidated Balance Sheet, as of May 31, 1969 (SEC report):

Assets	
Cash	$101,869
Receivables	404,857
Inventories	208,329
Prepayments	109,986
Total current	$825,041
Net prop., etc.	1,750,242
Other assets	96,284
Total	$2,671,567
Liabilities:	
Notes, etc., pay.	$161,192
Accts., etc., pay.	593,868
Fed. inc. tax	144,399
Total current	$899,459
Notes payable	$506,360
Def. Fed. inc. tax	97,353
Minority interest	18,052
(1)Com. stk.	332,560
Retained earnings	817,783
Total	$2,671,567
Net current assets	d$74,418

SPAULDING BAKERIES, INC.

History: Incorporated in N. Y. August 16, 1926.

Business: Operates bakery selling bread, rolls and krullers in N. Y., Conn. and Pa. under name County Squire.

Income Account, yrs. ended:

	Dec. 27,'69	Dec. 28,'68
Sales, etc.- - - - - - - - -	$10,796,167	$10,904,022
Cost of Sales- - - - - - - -	6,071,326	6,097,757
Sell., etc. exp. - - - - - -	3,966,249	4,026,198
Interest - - - - - - - - - -	48,357	50,351
Income taxes - - - - - - - -	387,832	390,536
(1)Net income- - - - - - - -	322,403	339,180
Prev. retain. earn.- - - - -	1,747,549	2,626,935
Dividends- - - - - - - - - -	218,566	218,566
Retained earnings- - - - - -	1,851,386	1,747,549
Earn., com. share- - - - - -	$0.77	$0.81
No. of com. shs. - - - - - -	420,320	420,320

(1)After $264,895(1968 $249,900) deprec.

Assets: Balance Sheet as of:	Dec. 27,'69	Dec. 28,'68
Cash & equity	$123,398	$260,076
U.S. Treas. bills- - - - - -	780,645	544,947
Receivables net- - - - - - -	467,264	406,470
(2)Inventories - - - - - - -	257,257	226,643
Prepayments- - - - - - - - -	154,479	153,196
Total current - - - - - -	$1,783,043	$1,591,332
(1)Prop., etc., net- - - - -	2,635,298	2,782,224
Cash val. life ins.- - - - -	48,454	61,181
Mkt. secur., cost- - - - - -	4,425	4,525
Other assets - - - - - - - -	49,809	61,875
Total - - - - - - - - - -	$4,521,029	$4,501,137
Liabilities:		
Accts., etc. pay.- - - - - -	$481,342	$514,829
Accruals - - - - - - - - - -	27,302	18,732
Dividends pay. - - - - - - -	92,470	92,470
Income taxes - - - - - - - -	66,685	40,645
Other curr. liab.- - - - - -	17,847	18,361
Total current - - - - - -	$685,646	$685,037
Long term debt - - - - - - -	752,900	837,600
Def. inc. taxes- - - - - - -	180,297	180,151
Capital surplus- - - - - - -	1,050,800	1,050,800
Retained earnings- - - - - -	1,851,386	1,747,549
Total - - - - - - - - - -	$4,621,029	$4,501,137
Net current assets - - - - -	$1,097,397	$906,295

(2)Lower of cost (fifo) or mkt. (3) 420,320 no par shs.

COURT CASES

Case No. 9. *Drybrough v. United States*[12]

Issue: Substantial discounts from fair market value of real estate holdings allowed for minority interests

Purpose of Valuation: Gift tax

Valuation Claimed by Petitioner	*Claimed by IRS*	*Final Adjudication*
$134,328	$526,800	$171,452

Supplementary Information: Parcel of real estate and four closely held realty corporations holding six parcels of real estate, four parking lots, and two smaller pieces of property

Issues Argued

Although there were other issues involved, the principal one was the valuation of gifts made in May and June 1957, by Mr. and Mrs. F. W. Drybrough to their son. The gifts consisted of an undivided 40% interest in real estate located in Louisville, Kentucky, and 40% of the issued and outstanding capital stock of four real estate holding corporations. The parties agreed that the value of the underlying realty comprising the sole assets of the corporations must be determined and the mortgage indebtedness, if any, should be deducted therefrom, and that 40% of the resulting figure is the "book value" of 40% of issued and outstanding capital stock of the individual corporations. Both sides produced qualified experts and filed briefs summarizing their valuations. The gross valuations of the underlying properties (before deducting mortgage indebtedness of $749,000) of the respective parties and the court were as follows:

	Plaintiff	Defendant	Court
Parcel of land	$ 238,750	$ 238,853	$ 238,000
Properties held by corporations	1,006,400	1,314,220	1,142,000
Total	$1,245,150	$1,553,073	$1,380,000

[12] 208 F. Supp. 279 (W.D. Ky. 1962).

The next and important issue was what discounts, if any, were to be applied to the undivided interest in real estate, and to the minority interests in the corporations. The government contended that no discounts should be allowed, whereas the witnesses for the taxpayer testified to the contrary. They testified that a discount ranging up to 40% should be allowed on the undivided interest in the parcel of land. One witness for the taxpayer testified that a holder of minority interests in Kentucky corporations cannot control policy, dividends, or liquidation, and therefore such interests are not readily marketable. He suggested a discount on the "fair market" value of the 40% interest in the corporations ranging from 33⅓% to 50%. A witness for the government proposed a discount of "approximately 20%."

Decision

From a consideration of all the testimony the court concluded that the value of the undivided interest in the unincorporated real estate should be discounted 15%, and the minority interests in the corporation 35%.

Case No. 19. *Inga Bardahl*[22]

Issue: Low valuation approved for minority interest, based on discounts for lack of marketability and one-man management

Purpose of Valuation: Gift tax

Valuation Claimed by Petitioner	*Claimed by IRS*	*Final Adjudication*
$286,000	$400,400	$286,000

[22] 24 T.C.M. 841 (1965).

Supplementary Information: Bardahl Manufacturing Corporation—manufacturer and marketer of oil and grease additives

Issues Argued

Ole Bardahl and his wife Inga Bardahl made gifts of Bardahl stock aggregating 2,860 shares to their daughters and grandchildren in 1959. In gift tax returns filed they valued such shares at $100 each. As of December 30, 1959, immediately prior to the gift here involved, there were 20,000 shares of Bardahl stock outstanding, over 85% of which was owned by Ole Bardahl.

The Commissioner, in his notice of deficiency, determined that the fair market value of the Bardahl stock transferred by gift was $140 per share.

Testimony developed that all of Bardahl's operations were under the direct personal supervision of Ole Bardahl, including manufacturing, marketing research, sales, and contacts with distributors.

The petitioners produced an expert witness who valued the Bardahl stock at $68.615 per share. The government's witness, a valuation specialist with the Internal Revenue Service, valued the stock at $132 per share. Incidentally, the book value per share of the stock was $96.57 on December 30, 1959.

Decision

The court found that there were insufficient sales of Bardahl stock to establish its value. Both the petitioner's and the government's experts relied on the price-earnings ratio of two competitor corporations whose stock was publicly traded. The ratio thus derived was applied to the weighted average per-share earnings of Bardahl for the five years ending with the year of gift discounted by the government's expert by 20% for the cost of floating a stock issue to the public and 10% because Bardahl is a "low diversification manufacturer, its products being related in nature and usage, which fact increases the vulnerability to competition and creates a sensitivity to savings in the business cycle." The petitioner's expert used the same 30% discount and "assigned an additional 20 per cent discount because of the one-man management of the corporation and the minority interest being valued."

The court felt that the government's expert should also have discounted his value for "the one-man management of the corporation" and the fact that a prospective buyer would consider anticipated earnings, particularly since available data indicated a decline from the high point achieved for the year of gift.

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TWO STEP ACQUISITIONS

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	Initial Date	Price	Percent Acquired
IPL Corp. - U.S. Consumer Prod.	12/65	$5,000,000	90%
LTV Electrosystems - Mercor Inc.	1/67	1,500,000	33%
General Aniline & Film Corp. - Ruberoid Co.	5/67	33,000,000	26%
Pennzoil Co. - United Gas Corp.	12/65	225,600,000	42%
Glen Allen Corp. - Phillip Carey Mfg. Co.	2/66	11,300,000	23%
U. S. Smelting, Ref. & Min. Co. - Mueller Brass Co.	3/65	20,300,000	92%
Diebold Inc. - Lemson Corp.	6/65	7,300,000	90%
Philadelphia & Reading Corp.- Lone Star Steel Co.	8/65	64,300,000	73%

TWO STEP ACQUISITIONS

50

(discounts for minority interests)

Approximate Asset Size of Acquired	Subsequent Date	Price	Percent Acquired	Price For each 1%	Minority Interest Indicated Discount
$100,000	5/66	$3,200,000	4%	$78,050	22%
45,000	4/67	5,900,000	67%	88,100	97%
1,150,000	5/67	90,000,000	74%	1,220,000	6%
9,370,000	1/68	618,000,000	59%	10,660,000	90%
423,000	6/67	37,800,000	72%	525,000	25%
243,000	9/66	3,700,000	13%	285,000	17%
86,700	7/66	600,000	10%	60,000	31%
877,000	4/66	17,900,000	27%	668,000	24%

Ave.	31%
Ave. w/o High-low	24%

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UNITED STATES TAX COURT

SEYMOUR SILVERMAN, ET AL
Petitioner

vs

COMMISSIONER OF INTERNAL REVENUE
Respondent

DOCKET NO. 3707-72
3708-72
3709-72
3710-72

LOCATION OF HEARING: NEW YORK, NEW YORK

DATE: March 27, 1974

BEFORE: THE HONORABLE WILLIAM H. QUEALY

APPEARANCES:

SIDNEY GELFAND
WALLACE MUSOFF
for Petitioners

STANLEY J. GOLDBERG
for Respondent

The $17 a share alluded to by counsel is when there was only 2,000 shares common stock -- I think even less than 2,000 shares of common stock outstanding and there was no -- 25,200 of preferred requiring 126,000. In other words the $17 might have been 34,000 or 28,000 or 17,000 dollar dividend. Subsequently, we have requirements on the preferred stock of 126,000 and there were no dividends then on the common. Just as background, Your Honor.

Mr. Jack Silverman, will you take the stand.

THE CLERK: Raise your right hand. Do you solemnly swear that the testimony you are about to give in this case to be the truth, the whole truth and nothing but the truth, so help you God?

THE WITNESS: I do.

THE CLERK: Please be seated. State your full name and address for the record.

THE WITNESS: Jack Silverman, 847 Ivy Hill Road, Woodmere, New York.

J A C K S I L V E R M A N, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Silverman what was your position in Modern Maid Food Products Inc. in 1968?

A I was the President of the Corporation.

Q And your position today?

A The same.

Q It has been stipulated there was a recapitalization of Modern Maid Food Products Inc. in 1968. What was the purpose for that recapitalization?

A We are in a highly competitive business and the thought occurred to those in administration to solidify the employment of key employees. And for that reason we thought it advisable to offer a, a sale of stock, non-voting, and a -- also an intent on our part to have these people retain a small interest in the corporation.

Q Were you or the people who owned the stock at that time also interested in receiving a fixed return on part of your investment before the employees were to receive anything?

MR. GOLDBERG: Objection, Your Honor, that's a leading question.

THE COURT: Restate your question.

MR. GELFAND: All right.

BY MR. GELFAND: (Resuming)

Q Were there any other reasons pertaining to, uh, the receipt of a fixed -- to receipt -- were there any other reasons why the reorganization took place -- recapitalization took place?

A Well we -- I personally wanted to insure my fixed

investment and at the same time offer the employees who were with us a interest in the business but certainly not to have any ultimate say in the running of the operation.

Q When did you first advise the employees, the corporation was going to offer them an opportunity to buy stock in the company?

A After we received word that the recapitalization would take place and we thought we would offer them the stock when it would be a non-taxable -- or the stock would not be subject to tax.

Q We have stipulated the corporation sold the total of 4,790 shares Class B common stock at $10 a share to 17 persons. How was this figure of $10 a share determined?

A I thought it was a fair value based upon the book value of the company and the fact that there were no dividends, it was a good return, ultimately.

Q When did you decide to make -- no, pardon me -- did you consider or intend the Class B common stock sold by the corporation at $10 a share to be in the nature of compensation?

A No.

Q Did the corporation claim any deduction on its income tax return as compensation or otherwise for any possible excess value of the stock over $10 a share?

A No.

Q Will you please describe the nature of the business of Modern Maid Food Products in 1968.

A Modern Maid Food Products is categoried as a food processor. We have two divisions, one of which is manufacture of prepared flour mixes for baking purposes, which is known as the Food Service Division. The second division is that of the Food Processing Division where we manufacture, the terminology is breading and batter mixes sold to frozen food processors.

Q Would you please --

A The Food Service Division distrib -- manufactures and distributes its products to eating places, ultimately. The Food Processing Division ultimately distributes its product to frozen food processors.

Q Will you please explain what you mean by a prepared flour mix.

A A prepared flour mix is one that is made from a base of all raw materials in dry form to which only water would be added for baking purposes.

Q Who are your competitors in the prepared flour -- Who are competitors of Modern Maid in the prepared flour mix field?

A It can be categoried as Pillsbury Flour Mills, and General Mills, D.C.A. Food Industries, they are the major ones.

Q Was there -- Who are your competitors in the breading and batter mixes?

A In that category we have Newly Wed Baking Co. of Chicago, we have D.C.A. Food Industries, and also the Griffith Laboratories of Toronto, Canada.

Q D.C.A. Industries, was that previously known under any other name?

A It was known as Donut Corporation of America.

Q Was there any agreement attached to the Class B Common Stock that was the subject of gift to buy the shares back if so requested? That is, the Class B stock that was subject to your gift, was there any agreement for the company to buy that back if -- or for you to buy it back, if requested?

A None that I recall with the possible exception of if employment terminated, or upon death.

Q You don't know whether there was any agreement or not?

A I doubt -- I doubt if there was.

Q Did the Class B Common Stock have any right by agreement or otherwise to have representation on the Board of Directors, or a voice in the management, business policy, or dividend declaration?

A No.

Q Up to and including the date of your gifts of the Class B Common Stock of Modern Maid Food Products Inc., were there any negotiations or agreement for the public sale of any securities for the merger or sale of Modern Maid Food Products, Inc.?

A No.

Q Up to and including the time of the gifts, did you have any intention for Modern Maid Food Products Inc. to become a public owned corporation, or to merge or sell said corporation?

A No, there was not.

Q During the summer of 1968, did Modern Maid Food Product -- was there any impending dramatic change in the operation of Modern Maid Food Products Inc. as the result of any invention, new products -- new process or acquisition?

A No.

Q One moment please. Mr. Silverman, Modern Maid Food Products Inc. did go public in October 1969, 14 months later.

A Correct.

Q When did you have your first negotiations with the underwriters or any underwriters in connection with that public offering?

A It was in March of 1969.

Q All right. Will you please explain to the Court

what -- how that arose and what occasioned it?

A Well the year 1968, the latter part of 1968 saw an expansion in our business. We were looking for new fields to conquer so to speak because our present facilities were running to capacity. We were looking for a plant to be built either in the Midwest or possibly in Canada. Canada became very attracted to us at that time because we had the opportunity of purchasing a flour mill in Streetsville, Ontario. That mill was known as Reid Milling Company. The approach was made to us by their President, Mr. Paul Helliwell, to possibly negotiate the purchase of the mill or else put up a plant for breading and batter mixes right along side their operation in Streetsville, Ontario. That gave us the thought of the need of a -- increased capitalization or increased monies should be -- have to put up one or two more plants because the demand for our product was growing nationwide and we found it difficult to fulfill it -- fulfill the demand with the current facilities we had at that time.

Q How did that -- when then -- how did that lead to the discussion of going public?

A Well, my son Stanley, who was in conversation with friends of his and others, discussed our problem and the thought was given to him and he brought it back to me in early '69 of why don't we look into the possibility of going public. He had spoken to somebody and this party

brought him together with, ultimately, the underwriter.

Q Excuse me one moment, Your Honor.

(pause)

Q Mr. Silverman, could you identify this book please.

A These are the minutes of our Board of Directors meetings, of Modern Maid Food Products.

Q All right. I turn your attention to the minutes of Dec -- the 6th day of December 1968, particularly with regard to the bottom paragraph -- oh yes -- May I have this marked for identification.

** THE CLERK: Petitioner's Exhibit 15 marked for identification.

BY MR. GELFAND: (Resuming)

Q Does Exhibit 15 for identification refresh your recollection when you had these discussions with reference to Reid Milling in Canada?

A Yes, this has reference to our discussion and the Board of Director meeting so indicate. Can I read it?

Q Not yet. Is this the time that you had the discussions that led to the requirement for the fund for going public?

A This was about the time we presented it to the Board of Directors and a decision made to seek other plants for activity and ultimately seek a public issue for the needed funds.

MR. GELFAND: I offer this page in evidence. I want to make a photocopy of it.

MR. GOLDBERG: Respondent has no objection to this Your Honor.

** THE COURT: It will be received.

(Whereupon, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 15 was received in evidence, as described above.)

MR. GELFAND: Your Honor, may I retain this --

THE COURT: You may substitute --

MR. GELFAND: And then substitute a photocopy.

BY MR. GELFAND: (Resuming)

Q Mr. Silverman, will you now read this para -- last paragraph on the page of the minutes of December the 6th, 1968.

A A discussion followed as to the plans for expansion into the Canadian area and particularly with respect to the serious talks underway with Reid Milling Limited. It was pointed out that the Corporation may be required to make a substantial investment, since the operation in Streetsville, Ontario Province of Canada, will involve the construction of a building and the necessary equipment for a breading operation.

In view of the heavy expenditures involved in the modernization of the existing plant, it may become necessary to arrange some financing before proceeding with the Canadian proposal. In any event, all problems associated with it are being checked out and there will be shortly -- there shortly will be a conference in New York with the representatives of Reid Milling Limited to move this matter. The Directors authorize Jack Silverman as President to enter into such preliminary agreements as he may deem necessary for the purpose of concluding this project.

Q Thank you.

MR. GELFAND: No further questions, Your Honor.

CROSS EXAMINATION

BY MR. GOLDBERG:

Q Mr. Silverman, would you say your company was a --

THE REPORTER: Would you stand --

MR. GOLDBERG: Is this one working?

BY MR. GOLDBERG: (Resuming)

Q Mr. Silverman, would you categorize your company as an expansion minded one?

A Today it is.

Q Or even in 1967 and 1968?

A In '68 it became one, yes.

Q Had your sales and profits substantially increased over the last 4 or 5 years prior to 1968?

received in evidence, as described above.)

MR. GOLDBERG: Thank you very much, Your Honor. The respondent will substitute copies of this.

BY MR. GOLDBERG: (Resuming)

Q Mr. Silverman. back in 1968, in June, when you had your first recapitalization and you created the B shares of common stock, you testified that one of the purposes was to solidify the employment of certain key employees. Is that correct?

A Right.

Q And you sold approximately 4,700 I believe you stipulated --

A 4,790

Q 4,790 shares of this B stock to both employees and, I see in the stipulation, also to Arthur Jaspan and Joseph Jaspan. Could you tell me who these two people are?

A They were our counsel, company counsel.

Q Did you also execute a buy, buy-back agreement with them also?

A Yes.

Q Why was there a need to create approximately 91,000 shares of B stock, non-voting stock, when you -- when you only sold approximately 5,000 to, to these people we've stipulated to, either employees or your counsel?

A The 17 or 18 people who were involved were -- the stock was sold to these individuals for the prime purpose of ensuring their employ and relationship with our company; it had nothing to do with the 91,000 shares you referred to.

Q Did you intend to make large gifts of stock to your children at the time?

A At that time, we did.

Q And, uh, is Seymour Silverman your brother?

A He is my brother.

Q Do you know at the time he also made substantial gifts to his children?

A That's right.

Q Why didn't you have any buy-back agreement executed between the trustees for your children and yourself, like you did for the other 49 or 4,790 shares of stock?

A At that time one of my children was not in our employ and it was a gift to my children. ultimately if they should carry on the business.

Q So you intended them to have a, an ownership interest in the business?

A Ultimately, yes.

Q Ultimately. Why must -- Have you bought back any of the 4,790 shares of stock to date?

A No. No.

Q Did your company pay dividends on the B stock, or

67, wanting to buy this company?

THE WITNESS: Yes, sir. We've had many approaches from larger companies to purchase our or acquire our company.

THE COURT: Seapack or Ocean Products, or Booth Fisheries, any of those?

THE WITNESS: Booth Fisheries subsequently was taken over by Consolidated Foods and although many inquiries were made, we thought it not desirable to sell to a customer who would find it difficult to maintain their status in the field. But many other larger companies have made approaches to purchase ours. We listened but never entertained any ultimate decision because we wanted --

THE COURT: Well, was any offer ever made to you?

THE WITNESS: No, not directly by way of net dollars and cents.

THE COURT: In other words, you never got to the -- got to the stage of how much? --

THE WITNESS: That is right.

THE COURT: Anyone would be willing to pay for the company?

THE WITNESS: No, never.

THE COURT: Thank you, Mr. Gelfand.

MR. GELFAND: Thank you, Your Honor.

REDIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Silverman, were you interested in selling your business, or you were interested in preserving it for your sons?

A I was interested in preserving it for my sons and I still am.

Q Uh, when the possible need for additional funds arose in late '68, early '69, in connection with Reid Milling, was it -- was the first thought of going public or did that subsequently come out? In other words, were you interested in financing or were you interested in going public?

A We are always of the opinion that whatever expansion was necessary in our business we could do it from internally, but when it came to a point of putting up a new plant, we thought not to use our own funds and to go to a public issue, as was suggested by -- to my son that it was the wiser thing to do.

Q Did you look for the public issue, or was this suggested to him as a possibility?

A It was suggested to him in conversation with one of his friends who ultimately suggested he go to see a certain underwriter.

Q Prior to the time your son, Stanley, brought the idea of going public, what type of financing were you contemplating?

A We weren't seeking any outside financing. We, we

didn't contemplate any financing, excepting if we had to build a plant, we thought of going to a banking institution. But the advice submitted to us was not to go that direction.

Q You talked about expansion of your business in 1968, do you recall whether that took place in the early part '68 and the latter part of '68, apparently your conversations with Reid Milling you said took part in the latter part of '68 --

A That is right.

Q By the latter part, maybe I can refresh your recollection -- Can you tell me what this is Mr. Silverman?

A This is a reply as --

Q No, just what is it?

A This is a Reid Milling letter to us based on a visit we made in Canada --

MR. GELFAND: May I have this marked for identification?

THE CLERK: Petitioner's Exhibit 16 marked for identification.

BY MR. GELFAND: (Resuming)

Q What is the date of this letter?

A October 26th, 1968.

Q All right. Does that recall to you when you first had your first conversation with them or conference with them?

A It was shortly before then that we spoke on the telephone, that was Mr. Helliwell and myself, and then we

arranged for this visit in Canada.

Q And the date of this visit in Canada was October 26th, 1968?

A The date of the visit was, I think, October 14th, two days prior.

Q Two days prior All right.

MR. GELFAND: I'd like to submit this in evidence please.

MR. GOLDBERG: I have no objection, Your Honor.

THE COURT: It will be received.

(Whereuppn, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 16 was received in evidence, as described above.)

BY MR. GELFAND: (Resuming)

Q Mr. Silverman, after December 31st, '67, were there any financial statements prepared for you up to the time of the gifts that you made? In other words we have a financial statement of December 31st, '67?

A Right.

Q Did you receive -- were there interim audits, interim financial statements, or did you get them just once a year? Shaking your head doesn't say anything.

A I'm sorry. No, there were none prepared that I

know of.

Q All right.

A Excepting the Annual Report which was December 31st.

MR. GELFAND: I have no further questions, Your Honor.

RECORSS EXAMINATION

BY MR. GOLDBERG:

Q Just two very brief questions. Mr. Silverman, if the price is right would you have sold your company?

A I can say that by saying any price, anything is for sale at a good price.

Q I see.

A The question is, what was the right price?

Q What would you sell your company for?

A I can't answer that right now.

Q But you would be willing to sell it, if the price was right?

A There'a a price for anything. I say, yes, it could be sold, but I can't tell you now what I would get for it.

Q Uh, I believe there's a letter in evidence back in October --

MR. GELFAND: He has it, the last exhibit.

MR. GOLDBERG: The last exhibit.

BY MR. GOLDBERG: (Resuming)

Q Dated October 26, 1968, from Reid Milling, -- how did you learn about Reid Milling and their -- in this deal?

A I mentioned earlier that in that period, or prior to then, there was a telephone strike in Canada and I recall distinctly that -- I'm sorry, there was a mail strike, a mail strike in Canada, and Mr. Helliwell called me on the telephone indicating that he would want to get in touch with us, but mail being so slow and he indicated that he would call on the phone to see if we were interested in a joint venture. I told him a joint venture at that time would not be what we were looking for, but we would be glad to speak with him, perhaps to either buy his mill or put up a plant near his mill. That ultimately led to the first visit in the latter part of October 1968.

Q How were you two people brought together? Was there a broker?

A Just by -- no.

Q Just by word of mouth or by --

A Just by, call it coincidence, he just called us on the telephone and it opened our thinking that we should perhaps entertain a proposition of that kind, inasmuch as one of our major competitors, as I listed earlier, Griffith Laboratories, had a plant in Canada.

Q Have you done any business with Reid Milling prior to this time?

A Never.

Q Have you -- did you hear of their reputation?

A I ultimately sought it out and found out what their reputation was.

Q Fine. So it was sometime prior to prior to October of 1968 that you --

A It was the early part of October, or during the middle of October that I sought it out.

MR. GOLDBERG: That's all, Your Honor.

FURTHER REDIRECT EXAMINATION

BY MR. GELFAND:

Q This telephone call that -- was that an unsolicited telephone call?

A Unsolicited.

MR. GELFAND: I have no further questions, Your Honor.

THE COURT: You may be excused, Mr. Silverman. Thank you.

THE WITNESS: Thank you.

MR. GELFAND: Mr. Witt.

MR. GOLDBERG: Your Honor, could we have a 5 minute recess.

THE COURT: All right, we'll have a 5 minute recess.

THE CLERK: Rise please.

(Whereupon the hearing in the above recessed at 11:20 a.m., as described above.)

THE CLERK: Would you spell your last name please.

THE WITNESS: (spelling) W-I-T).

H A R O L D M. W I T, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Wit, we have stipulated to your qualifications and business experience and I'm not going to ask you any questions with reference thereto. But could you summarize briefly the basis of your appraisal report. How you look at and evaluate shares of common stock of a company, similar to the Class B stock of Modern Maid Food Products Inc. and how you arrived at the value you have?

A I'd to say that I, I, -- I don't think the way -- if I -- the question is the way that, that I think about it. I -- As I said I'm with an investment banking firm and, you know, I am -- I am a principle and so that they way I would look at this would be, I think, the way I would look at it, you know, as a buyer at that time. And supposedly a willing and knowledgeable buyer. And as, as I understand the facts that the stock we're talking about, the Class B stock --

Q Pardon me, do you want a copy of your report in front of you?

A No.

Q You don't need it?

A No.

Q All right.

A That the Class B stock, as I understand it, -- in the first place the company was a private company then and the Class B common stock had no right, the holders had no right to vote for the election of Directors; had no right to notice of meeting; had no right to, to change the relevant corporate documents to give them such a right; they had no contract giving them any right to elect a Director of the corporation; they had no right, as I understand it, except informally to influence the business of the corporation in any way; and they had -- so they had no right to elect Directors; they had no right, as I understand it, the Class B stock to, to receive dividends by any charter document, except as I understand it, liquidating dividends pari passu with the Class A stock in the event of liquidation after payment of the, of the, of the Class, of the preferred stock dividend. As I understand the facts, that they preferred stock requirements after the so-called reclassification of 1968 were, whatever they were, were much greater than the combined total for dividends paid, both the preferred and common, prior to that date. And also, as I understand it, that after the recapitalization in 1968, no dividends were in fact paid on the common stock at any time.

Also, as I understand it, the, the -- at the time that we're talking about, or just prior to the time, there were no serious discussions, contracts that would indicate that the company was, was considering a public offering of its securities, or private sale of its securities to a, that's a third party buyer, such as any institution. There were no discussions or contracts relating to a possible sale of the company, a possible major purchase by the company of a major asset, or liquidation of the company.

As I also understand it, that at that time, there were no what I call no things going on that would have changed in a fundamental and radical way, or a very, you know, important way, the business of the company, either by entering into a new field that promised hopefully greater earnings of a new invention, or a new process that would in the view of someone like myself offer the prospect of a serious change in the dimension and the type of a business.

I also understand that, that somewhere in here, that. that -- that there were no Class B stock that that's under discussion here, there were no buy out or buy back arrangements, in other words there was no put arrangement by, by contract or by understanding with respect to that Class B stock.

And those of the, the, you know, the facts that would have come to me as a principle or as a possible advisor to

others, as to whether or not to buy stock like this.

Now, it would seem to me -- and also I understand -- I've been through the figures and I understand that at the time we're talking about, I guess in December of 1967, that the stated book value was something like $12.35 a share and undoubtedly was greater at the time, you know, when the gifts were made because the company was earning money.

And also, I understand from the figures in the prospectus and other things I've looked at that, that the, the average earnings, depending on how you play this game, different people look in different ways, were after preferred dividend on a pro forma basis which is the way you, you adjust these things, that if you take the 3 or 4 years prior you're talking about and average earnings, you know, of $4 a share, so that my own view of what I might pay for it, that is not more than $5 or $6 a share at the time, takes these things into account. It doesn't take into account the sort of things you'd have to have much more information about, which would be the quality of the earnings, you know, the, the actual assets on the balance sheet, you know, how you would view those, whether they were in fact stated properly and how you would discount them. But I don't really believe that for the sort of thinking that I've been trained to do about value that those things are particularly relevant.

So that I concluded in looking at it and based upon my way of looking at things and experience I have had that you'd have to take a look at this situation, it's a completely locked-up situation. I mean, with absolutely no right of a buyer of Class B stock to have anything to say about the business of the company, to change his condition in any way, to demand a public offering of stock, in any way to -- he'd have to be completely passive and hope that some day in some way that something would happen, either through a sale or a liquidation or a public offering, to give him some value to his stock. And I would say that, that a man who was a knowledgeable person and a experienced investor, that is one who, who sees a number of different things and who not only anticipates in investing that he's going to hopefully make some big gains but obviously take some losses along the way and also be locked up along the way, since we're talking here at the price that I think, you know, is a price that makes sense of I guess with even the smallest block of stock that was, that was given away, you know, $30, $40,000, given my prices, and the biggest block, the $125 - $130,000. That he would, in this situation, look to making ten times on his money and that would be what he would be looking for now, in this situation if he was looking for that, and taking those $4 earnings and taking the, the excessive valuations which Your Honor has stated, were given at the time, that he

would say, okay, here's a company that's earning $4 a share average, maybe it'll earn a little more and maybe it'll earn a little less, it's a good earnings record but, no know, not you know it's not startling like IBM or Polaroid or one of those things. That, okay, let's say that we go public sometime maybe and if the prevailing conditions are, which they were around 1968 for companies like this, you know 10 times, 12 times. Let's say we're talking about 12 times $4 or 4 and a fraction, we're talking about $48, no $50, maybe 10 times 5 is, you know, 50, perhaps $5 is a good number, $6. I mean, we're talking here, I think, about a way of thinking that is not subject to fine, statistical analysis. It's not subject to fine appraisal methods. It's a sort of thinking of what I might hope to get if all things worked out the way they might. And if the market conditions remain more or less the same and in a situation where I've absolutely nothing to say that will either make my investment liquid or give me something else that will compensate me for locking up my money, such as dividends, salary, and so forth. And I would say that, that as a professional investor that if there were other conditions that based upon, you know, my judgement of the people or the pressures on the business or financial pressures on the stockholders that would have said okay even though I don't have a contract, and even though I don't have an understanding, there's so much pressure on the

business that they've got to go public, sell out, or do something where I can see that my investment will become liquid. And in that case, I might have said, well I'm alright maybe, 6 times on what I've put in, or 5 times what I've put in, is a reasonable expectation. But certainly not, under the conditions, that, that seem to be present here which is a completely locked up situation with, with a company that with all due respects was, you know, a good company but a company that I'm sure was in a cut-throat competitive industry where I'm sure there were sales relationships, and no matter how much I investigated it, I couldn't find out what they were, about competitive situations which I'm sure, you know, I probably woulnd't have taken the time to do because of the, you know, amount of money involved. And that's generally the sort of thinking I would do, or would have done at that time considering what I thought this thing might have been worth.

Q Thank you, Mr. Wit. In addition to your own views as to how you would have invested, is that the way you were also advising others? I mean in situations that were coming--

A Well, I, I don't -- the, the -- My experience has been with a firm where we, it's not always the case, but, but in most instances we're the principles ourselves. And we're -- because of my employment relationship that, that we as

employees of the firm, if we bring in something, we expect to put our own money in it.

Q Pardon me, I misunderstood what -- When you said you, you for Allen and Company.

A No when I say I'm an employee of that firm that if, if, if a deal comes in that I am involved in, that is originated, work it up, if the firm or its associates in the firm put in money, I'm expected to put up my own, so that as a principle I think, you know, very carefully about, you know, it's my own money. I'm not just sitting there collecting the fee and you know smiling when the thing goes down drain; get another customer. It's my own money. It's the firm's money. And I've also, you know, had friends in deals and so forth. I've also had experience in pricing public deals and have been through the whole, I think, range, you know, investment possibility.

Q Were there actually deals made during these period of years on the basis you have just explained?

A Well, I'm sure -- Yeah, there were and, and certainly that mode of thinking about, you know, of trying to, and it's not very precise, of trying to, sort of discount risk which we're really talking about. Certainly I've done a lot of those. I've just sort of, I mean they're different types of things. There's nothing let's say exactly on point, but-- but the -- we've been in deals where we put money into compan-

ies that, that were locked up, you know, that had earnings, that had certain features about them. But I'd say that in each of those situations, and that's why this is sort of different and it's a hard thing for me to even put a value on, because I, you know, in each of those things, there was something involved in the deal, either formally or informally, that gave us the feeling that within a relatively short time, there would be liquidity produced either by, by reason of the, of the formal commitment, by reason of the, of the financial requirements of the business, or by reason of, of the temperament of the principles or the controlling people involved in the deal.

Q In other words, the valuation of $5 to $6 a share that you have in your report, that does presuppose going public or becoming liquid at some time?

A Well, I would say that, that -- I don't say presupposes going public. I'd say a man who has a, looks a lot, you know, has a lot of different investments, might say, well, you know, this looks like an interesting business; this looks like good people; you know, they have good earnings; there's a book value there; well, I'll put some money in it and, you know, maybe some day in some way, you know, something will happen; in the meantime, I can afford to sit there without any return or salary.

Q But when you say liquidity, you're referring to

a merger or a sale out of the business.

A Well. I'm -- liqudity I'm referring to something where somebody -- where, where at some point I can turn in this stock certificate for, for dollars. That's why I mean by liquidity.

Q Mr. Wit is this the report that you have prepared?

A It's my illegible signature.

Q And this sets forth the basis on which you arrived at your figure of $5 to $6 a share?

A Yes, sir.

MR. GELFAND: Your Honor, may I -- I'd like to submit, but I think we ought to mark the original in evidence.

** THE CLERK: Petitioner's exhibit 17 marked for identification.

** THE COURT: Petitioner's Exhibit 17 will be received.

(Whereupon, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 17 was received in evidence, as described above.)

THE COURT: Let me ask you, Mr. Wit, can you conceive of any circumstances under which you would recommend the purchase of this Class B stock at any price, unless there was something -- that you could get your hands on that would

indicate that at some stage of the game, why there would be a market in which you could resell it?

THE WITNESS: Well, I'd say, Your Honor, that depends a little bit on the time that we're thinking about. I think that, that if we're talking about the period of 19, you know, '64 or '65, 6, 7, 8, and perhaps into '69, that my view would be perhaps a little different than it is today because of the changed market conditions. And I would say that, that, you know, there might be a type of person around that time, and given the facts about that time, there were so many deals going on, so many mergers, so many sales, so many, you know, that a man, you know, with -- looking at something like this might say, well, no matter what they say, you know there is that possibility that that will happen. And consequently if I had sufficient money and didn't have to use, you know, that money for groceries that, you know, I'd say why not take a shot, you know, I mean, that cliche that we all use. But perhaps -- and, and now of course with, with the public underwriting market, you know, and the stock market changed so much, you know, probably wouldn't touch it with a ten foot pole. But at that time, you know, the, the atmosphere was different.

THE COURT: Can you account for the fact that a year later, and I don't think the market conditions were any better in '69 -- as a matter of fact, isn't it true that by

1969, the, the zest with which people expected to buy un, unseasoned securities and make fortunes had, had abated a little bit?

THE WITNESS: I'd say --

THE COURT: They'd been a few burned by then,hadn't there?

THE WITNESS: A few burned, but none killed and, and it had abated but it was like, you know, sort of like the last throes of fever, you know, there were still a few highs back and forth. And I don't think people really believed at that time, I mean, you know, that's my -- that it was all over. There was still, you know, these -- no one believes that such easy times aren't going to last forever.

THE COURT: Can you account for the, the ability of Ladenburg to market this stock at what amounted to an equivalent of about $75 a share?

THE WITNESS: Well, I mean without trying to be disrespectful to my profession, it's not really a profession but art, I, I don't really know, you know, who there customers were, or enough about there syndicate operation to be able to answer that in any, in any way. I, I do remember at that time that if one had a business that was -- that was -- that looked solid where it looked like they had a history of good earnings that, you know, what most underwriters would do, would say, you know, 10 or 12 times earnings and that

was sort of like the cliche of the time. And buyers unfortunately, you know, didn't really, you know, look carefully into the business and didn't make the proper comparisons and didn't do the hard thinking. If they had made money with a broker and the broker called them up and said, gee I've got this great thing coming out here and why don't you buy 300 shares and the man would probably say yes.

THE COURT: Was this about the time Nathan's came out do you recall?

THE WITNESS: I don't recall.

THE COURT: Mr. Goldberg.

MR. GOLDBERG: Yes, sir.

CROSS EXAMINATION

BY MR. GOLDBERG:

Q Mr. Wit, in your report you stated that, I refer you to page 4, that someone who would've invested in this company would have won an increase of, of about 10 times on his investment, in other words 10 -- $10 for every $1 he's invested.

A That would have been his expectation.

Q Oh, his expectations. How many people in the market really were able to meet their expectations?

A We're, we're not talking about the market. What we're talking about, as I understand it, is the state of mind of someone who is a willing buyer under those sets of

facts and what, what, what I as, as a person, you know, who was a principle with some experience would look to say if everything works out what would be -- what I would hope to get from this and then discount that back. Now, I think when I say a willing buyer, I'm talking about somebody who also knows enough to know that if he puts other money in things like this he's also going to lose it, all of it sometime. And I've put money in, you know, maybe about 15 to 20, you know, different types of deals and, you know, there've been several bankruptcies and several things haven't worked out, so when you're looking at this you're not just saying I expect to get all my investments this way. But if I do them all and I'm in a high risk business and if I average down then maybe if I'm lucky, I can average out, you know, maybe 2 times my money over a period of 3 years. That's what I'm really talking about. I'm not saying that --

Q In other words this, this was -- this is your advice for someone that would be investing?

A What is that, sir?

Q That you would want realization of 10 times --

A I would say --

Q Or 1000 %?

A Yes, sir. Yes, sir. Under the circumstances that I --

Q Over how many a year period would you expect this?

A Well it's not mathematical because and, and, you know, I think if you're experienced in the investing business you know that everything always turns out wrong and that your timing is always wrong and that the things you expect don't happen, things you don't expect, happen. So that you can't be very precise. You look at these things and say, gee if it all works out maybe I'll make -- uh, put in 10 and get out 50. But I know that in the world it doesn't work out that way and maybe three other things I put my money in I lose it or make 2 times or, you know, make 1 time and get it back after 5 years. So I'd say it's sort of an averaging.

Q So in other words, an investor would be very happy to get 25% return every year, or growth on his investment?

A I think we're talking about different things. I think that we're about here a different type of investing than the man who goes into the stock market where he has liquidity. I mean, liquidity to me is a vital, vital element here. And if a man goes into the stock market, I mean they used to say a few years ago that the best investors would look to get 20% compounded on his money before taxes. And that was, you know, fabulous, you know, investing if a man could do that. But here I think we're talking about a different dimension of investing. We're not, we're not talking about buying stocks on the market, we're talking about a private, locked-up, you know, position that doesn't have

liquidity, that doesn't have dividends, that doesn't have, you know, any way that the man can get his money out, aside from going to the principle and holding a gun up to his head.

Q Did you have -- what resource data did you have when you made your report? Did you --

A What, who?

Q Resource data?

A What's that mean?

Q Oh, financial data, statistical data, anything, I mean how did you --

A I don't think the financial data means a damn thing in this sort of thing. Excuse me.

Q Did you speak to Mr. Silverman at all?

A No, sir.

Q Would you say this was a particular -- was this a growth company?

A Well I'd say it, it, it was a company that, that's why I said in, in the conditions of, of looking at it that it didn't seem to me from looking at the prospectus and, and the facts I knew that there was anything at the time that would show a dramatic increase in the earnings or the possible earnings of the business. In other words, if they had had for example a new patented method of, of -- I don't know what they could do here, but -- I'll say reducing the bulk of shipping, so that they could save 30% on the shipping

rates and kill all the competition, that would have been something that would have been existing at the time that would have made, in my view, the earnings seem less relevant. And maybe if they had a new invention that I would've said well, well heck the earnings don't really make any difference and, therefore, the price, you don't have to relate as much to a hypothetical price earnings ratio, which you're going to capitalize and then figure out backwards, you know, what your dollar of investment might be worth if this, this, this might happen.

Q You consider this a solid, solid company, don't you?

A Not particularly.

Q You don't consider a growth of between, of over 4 years of 46 cents to 83 cents a share an interesting growth pattern?

A Well, no, no, -- I -- I do, but I don't -- I didn't mean to, you know, any disrespect to Mr. Silverman and his associates, but this is not Quaker Oats and this is not Pillsbury Flour, this is one man, you know, in a family business over in Brooklyn sort of beating his brains out trying to increase his sales every year and it's not, I would say, in the spectrum of investment possibilities -- what I would call a, a -- since I'm being -- a quality company.

Q Well does General Motors double their sales in

four years?

A Sir?

Q Would a company like General Motors double their sales in four years?

A Well we're talking again about, I think, quality, earnings and growth. I'm not trying to be -- I agree the earnings did go up and therefore someone looking at it might have had a, a expectation of increasing earnings. But as I say, that, that I haven't, you know, didn't go in deeply into the quality of the earnings in that sense. How many customers there were, how much it cost to get in the business, what the competition might be, whether Pillsbury if they, you know, blew their nose could blow these fellows out of the, you know, out of the dock. I don't know.

Q How are new issues generally coming out at this time, in 1968? Were a lot of new issues issued --

A They were coming out like minnows flowing out of the stream, sir.

Q Right, and some were selling at 30, 40 times earnings?

A It was -- I'd say that was so, yes.

Q And it was a very bullish stock market then, wasn't it?

A Everyone looked like the here after was with us.

Q Do you know what the, when the, the high was reached

on the Dow Jones average?

A No, sir. I'm not -- that's not my business.

Q Oh, would be surprised if the higher was reached in December of '68 with 179 --

A I really -- whatever you say, sir --

MR. GELFAND: Your Honor -- Your Honor, I move that we strike that. I mean Mr. Goldberg is not testifying.

THE COURT: He's asking a question.

MR. GOLDBERG: -- Mr. ah.-- Mr. Wit's in the stock market, in the investment --

THE WITNESS: No, no, no I'd like to explain, I'm, I'm not -- we, we do not, I don't -- except insofar as I run some family trusts in a family business. I'm I'm not -- I don't advise people to buy a hundred shares of General Motors or 200 shares of American Telephone for their mothers. I mean that's not the business I'm in.

BY MR. GOLDBERG: (Resuming)

Q What business are you in?

A Well I'm in the business of, I think I've stated of investing or making recommendations for the investment of, of the money of the firm and my own money in a variety of things which might include public --

Q In other words, your, in fact, in the sense of, you said a merchant banker?

A Well, that's -- yes, sir. And I've, I've also --

Q I see, and you're not a, you are not a --

A I'm not a stock broker.

Q You're not a stock broker?

A No, sir.

Q I see.

A And, and I've also been involved, as I say, in, in family, family investments and also been involved in, in a -- pricing and, and negotiating of various types of, you know, public transactions, that is underwritings, mergers, and so forth.

Q Did you know this company did have a prior dividend paying history?

A Yes, sir

Q Did you take that into consideration?

A Well as I understand it, that, that they, they -- when they recapitalized in 1968, they I think put $2,150,000 into preferred stock, of which they had under their charter a 5% dividend requirement. And that amount from the figures I got was greater, that is the 5% of the $2,150,000 or whatever it was, was greater than the amount of dividend they had paid on their prior preferred and common before this 1968 recapitalization. And that, as I understand from, from Standard and Poor's that the sheet I got that, that after the company went public, that is after the 1969 recapitalization, they did not pay any cash dividends at all on the common.

I don't know if that's accurate but that's what Standard and Poor's --

Q I don't know myself.

A That's what the Standard and Poor people say.

Q Isn't it true the only basic difference between the Class A and the Class B was the voting?

A As, as far as I know.

MR. GELFAND: Your Honor, we have stipulated the Charters of the company on the recapitalization in '68 which specifically sets forth --

THE COURT: I assume that's, that he's preparing to lead up to another question, I guess --

BY MR. GOLDBERG: (Resuming)

Q So the only difference you say in -- the only difference in the -- in the two different classes was the fact that one was voting and one was not voting, is that correct?

A As I understand it, that was the formal difference. Yes, sir.

Q All right. You used a -- in your report you say that your pro forma earnings would have been $4.71 a share for 1967 and using a multiple of that time of 10 to 12 times earnings which would -- you'd recover something like $47 to $50 a share and you've discounted it all the way down to 5. So, ir other words, you have about a 90% discount for the

MR. GELFAND: Just one question.

FURTHER REDIRECT EXAMINATION

BY MR. GELFAND:

Q Do I understand that the question of liquidity versus locked-in position is the most important factor in making an investment in a closely held company?

A It is the most factor in, in not making an investment, or --

Q No, in making the investment, the question of liquidity or the question of being locked in.

A Well, I'd, I'd say that, that it's certainly the, the first thing that comes to mind, uh, you know, I think the mentality of the, of the -- of the sophisticated investor is that, you know, if, if he goes into the market and he buys shares of a company with, with a quoted market and he doesn't buy sufficient numbers so that he feels that he can't get out, then he always, you know, feels he could barring disaster, he can take his stock certificate, give it to someone, and get some cash money in his pocket. And I think that's a lot different than in a situation where you're sitting there with your, your, your stock certificate and you've got no place to go and there's no, no money coming in for holding this thing.

MR. GELFAND: I have no further questions, Your Honor.

THE COURT: Thank you Mr. Wit.

THE WITNESS: Thank you. Oh --

MR. GOLDBERG: Uh, just, just -- just one very brief question.

FURTHER RECROSS EXAMINATION

BY MR. GOLDBERG:

Q In other words, you've made your approach on the basis of a sophisticated investor, I gather?

A Oh, that's a little presumptuous, but I suppose --

Q Aren't you sort of narrowing your a, your field?

A Well, I -- No, I, I, I was understood that, that what I was asked was a willing and knowledgeable investor.

Q A willing and knowledgeable investor.

A And, and -- and that a willing and knowledgeable investor was, was one who, who had -- wasn't just the local dentist but was, was somebody who, who had seen a number of investment possibilities of different types and who had a choice about whether to put his money in a -- I assume he's in that business -- and, and, this is the one or another one, or another one and felt also that if he put money in this one that, that, you know, the next day, the next week, he'd have other opportunities.

Q So in other words this is not the, the general public in the sense that -- the buying public for stock. This would be --

A Well because the general public doesn't buy this

sort of thing. This is special business, specialized business in my view.

Q Isn't -- would you say that at this particular time in the market you probably could sell almost any, anything that is coming across the board.

A I'd say at that time, you know,if, you know -- you could even have sold a dead cat, you know, without earnings.

MR. GOLDBERG: Thank you. I have no further questions.

THE COURT: Thank you, Mr. Wit.

THE WITNESS: Thank you, sir.

THE COURT: Do you want to go ahead gentlemen, or do you want to recess now, or -- I guess you have --

MR. GELFAND: We might as well recess for lunch, Your Honor.

THE COURT: Yes. Do you think you can get back by 1:30 or --

MR. GELFAND: Yes, Your Honor.

THE COURT: Is that enough time for you, Mr. Goldberg?

MR. GOLDBERG: Oh, plenty, it'll be sufficient.

MR. GELFAND: Yeah, you go right upstairs, it's easy.

THE COURT: We'll, uh, we'll recess then until 1:30.

THE CLERK: Rise please.

A F T E R N O O N S E S S I O N

THE CLERK: Be seated gentlemen.

THE COURT: Call your next witness, Mr. Gelfand.

MR. GELFAND: Mr. Smith, please.

THE CLERK: Raise your right hand. You do solemnly swear that the testimony you are about to give in this case to be the truth, the whole truth and nothing but the truth, so help you God?

THE WITNESS: Yes, sir.

THE CLERK: Be seated. State your full name and address for the record.

THE WITNESS: Gordon Smith, 29 Neville Street, New Shrewsbury, New Jersey.

G O R D O N S M I T H, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Smith, we have stipulated your qualifications and background as set forth in your appraisal report and we shall not go into it at this time. I wonder if you could summarize briefly the procedures adopted and the basis for your valuation and how much it was for the Class B common stock of Modern Maid Food Products Inc. in August and September of 1968.

A Yes, sir. The approach I adopted in this appraisal was to value these shares on the basis of information I could gather that was publicly available concerning the prices paid of similar securities in the market.

The first step in my examination was to determine whether, in fact, there were securities of publicly traded companies, uh, being sold in a public market of companies which were comparable to Modern Maid. My search indicated that there were not, in fact, any companies which were truly comparable to Modern Maid in, in size and in nature. I did, however, look at several companies that I've cited in the food industry, more particularly manufacturers of consumer goods in the grain products area. I did this to satisfy myself that this particular industry was not being viewed by public investors as a special situation. That it was not a so-called glamour stock or in a depressed market. I did so satisfy myself and I concluded after some examination of, of Modern Maid's financial and operating data for, uh, for the years that I had available to me that I've, uh, cited in my report. I concluded that an appropriate price to earnings ratio for Modern Maid stock if it were on a public basis would be 10. This was based on my practical experience with some consideration of the general conditions of the market at the time. I applied this price earnings ratio of 10 to the average earnings -- net earnings

of Modern Maid for the years '65 through '67. I felt that this is the information that would be available to a prospective investor in these securities. The value I derived by that was $6,160,000 which represented to me the fair market value of the equity of Modern Maid if it were being actively traded in a public market.

These securities are not in fact, or were not in fact, being publicly traded. It was a closely held company and I felt an adjustment was warranted to that extent. One measure of this adjustment which has been used is, is the costs incurred in the, the process of going public and offering securities to the public market, including underwriting, commissions, fees, legal fees, accounting fees, and the expenses of the management of the company during the, during the public offering period. I concluded that a discount considering those factors of 15% would be an appropriate adjustment for the non-liquidity inherent in the purchase of a closely held security. Applying this discount to the value that I previously derived, I arrived at an adjusted value of $5,236,000, which represents the fair market value of this equity with consideration of its closely held status.

Now this equity included some preferred stock at that time. I looked at some other issues of preferred stock in companies that, while they were not in a similar business

to Modern Maid, were -- had a rating, like this, this Standard and Poor's rating as a matter of fact, similar to what I thought that Modern Maid would carry if it were rated. The rating of triple B or double B. I found that these investors in these securities were requiring a 6.4 average return on their investment. Modern Maid carried a $5 or 5% return on its investment. Carrying this through in a calculation, I concluded a value of $80 per share, which is what an investor would pay in order to ins-- assure himself of a, of a 6.4% return, as indicated by the market. This would indicate that the value of the preferred shares of Modern Maid was $2,016,000. I subtracted that from the $5 million-odd dollars and arrived at a value for the common shares of $3,220,000. I utilized the number of common shares as 108,000 in my calculation and dividing that out, you get $29.81 per share on that basis. This to me is the value of the common shares of Modern Maid if an investor could purchase a minority interest in the closely held stock of Modern Maid of one single class of common stock with a typical rights of receiving dividends, voting rights and, uh, capital distribution.

This, however, is not a possibility with Modern Maid. This was a single class of common stock that we're appraising here that did not have these typical rights. So, again, I felt that an additional consideration should be made for

that fact. I looked then at the records of some of, of some other investment companies, or funds if you will, that were formed actually during 1968 who specialized in investments in restricted closely held securities. And I examined them, where I could for the value line, Development Capital Corporation, which had been in existence long enough to have purchased some of these securities and have some experience. And I compared the price that they paid for shares of restricted unseasoned small venture companies with, in particular cases, of the shares that those companies had issued which were free. In other words the fund was buying restricted shares where the company already had some publicly traded issues. And I compared on the date the price they paid for the, uh, restricted shares with those that the free shares were selling and I found that, uh, discounts ranged from 16 to 70 percent, with the average being 44. If I look at the, the upper-half of these, I found that half of the securities were over 40% discount and they had an average of 57. Now I considered also in examining these that the prospectuses of these funds and I noticed that in several cases the funds in purchasing restricted securities of unseasoned companies had sought to reduce their risk by, uh, at the time of purchase negotiating an agreement with the issuing company that at some future date they could force a registration and there would be a public market for their shares.

I found that some of the funds reduced the amount of this type of security which they would purchase. Both of which are ways that they sought to reduce the risk of really liquidity, as we heard Mr. Wit mention this morning. They sought to, to assure their liquidity in the future.

After consideration of these facts I concluded that a, an appropriate discount to be applied to the Class B common shares of Modern Maid would be 60%. I applied that discount to my per share price of $29.81 and the computed result is $11.92. I concluded, therefore, that the fair market value of the Modern Maid shares being appraised as of August and September 1968 as $12 per share.

MR. GELFAND: May I have this marked for identification, please. May we use the original, Your Honor.

THE COURT: Yes.

** THE CLERK: Petitioner's Exhibit 18 marked for identification.

BY MR. GELFAND: (Resuming)

Q Mr. Smith, is this the report you have prepared in connection with your appraisal of the Class B common stock of Modern Maid Food Products Inc.?

A Yes, it is.

MR. GELFAND: Your Honor, I submit this in evidence as Petitioner's Exhibit 18.

** THE COURT: It will be received.

(Whereupon, the above mentioned document, having previously been marked for identification as Petitioner's Exhibit 18 was received in evidence, as described above.)

BY MR. GELFAND: (Resuming)

Q Mr. Smith, you arrived at a figure of approximately $12 a share when you divided through by 108,000 shares, um, making allowance for the additional 4,790 shares that had been sold, so there was a total number of shares outstanding of 112,790, do you know what your appraisal value would have been?

A It would be approximately $11.50.

Q Referring to your report on page 9, on page 9, you state that a certain group of companies were most closely representitve of Modern Maid Food Product Inc. Would you please explain what you mean by most closely representative.

A Well, I feel that, uh, these companies are first part of the, the food industry, as I noted, and, and more specifically they are involved in the processing of grain products and to that extent I feel that they are representative of, of Modern Maid's business.

Q You mean those were the closest you could find

representative, you don't mean that they are, well -- Do you mean that they are most closely representative or that they are the most closely you could find?

A They're the most, most closely I could find. They're the best of a poor compromise, I think.

Q Referring to the last paragraph on page 12 and the top of page 13, does your valuation presuppose Modern Maid Food Products going public?

A Yes, it does.

Q All right.

A I have assumed that a prospective purchaser of these sha[illegible] would be betting, to use a word, that the company would, based on its size, its business, the, the general characteristics of it that anyone could know in a public way.

Q Suppose there was no intention of going public, would that fact have -- factor have of had an effect on your valuation?

A Yes, it would.

Q What effect would it have had?

A Well, as I say, I've assumed that an investor would assume -- would go on the basis that it would within 2, 3, or 4 years. Uh, if there were some assurance to the contrary, it would certainly have an effect, it would reduce it substantially.

Q Would you be able to say how much substantially, or how substantially?

A Well, in my opinion, uh, an assurance of that kind would place this stock in the class of a, of a highly speculative, uh security and, uh, I guess I would have to defer to those who are in the marketing area to know what a, a highly speculative issue might sell for.

Q I direct your attention to page 18 of your report, the second sentence in the second starting paragraph that starts on that page. Value Line has stated that it is a policy that at least 50% of the value of restricted securities in its portfolio must be the subject of a commitment from the Issuer to registerer at Value Line's request, the securities, under the Securities Act of 1933. Do you know whether any such commitments existed with respect to the securities listed in Table 3?

A No, I do not.

Q Did you in your appraisal assume that they did exist, that some of them did exist?

A Yes, I did. I assumed that there were some in there that did have such an agreement, but I don't know the exact number.

Q Referring to Exhibit 3 in your report, do the restricted securities listed there have a public market for their shares, I mean for the free shares?

A Yes, of the --

Q In other words, these are restricted val -- discounts that are obtained on stocks that were already being traded?

A Yes, I selected these from that portfolio for that purpose.

MR. GELFAND: I have no further questions, Your Honor.

THE COURT: Let me ask the witness -- Mr. White in, in making these a -- in allocating your residual value between the Class A and Class B, did you give any consideration at all to the fact that less than one year later when it became necessary to make a similar allocation in connection with the public offering that the ratio was 7 to 6.5?

THE WITNESS: I was aware of that allocation, uh, frankly I did not consider it, I did not know what the source of that was and why that decision was made at that time.

THE COURT: In other words, you made no effort to try and account for the disparity between what was presumably an arms length division of the residual equity at that time with, with your determination?

THE WITNESS: That's true.

THE COURT: Mr. Goldberg.

CROSS EXAMINATION BY
MR. GOLDBERG:

THE CLERK: Please be seated. State your full name and address for the record please.

THE WITNESS: Herbert S. Cannon, 140 Tekening Drive, Tenafly, New Jersey.

THE CLERK: Would you spell your last name for the record?

THE WITNESS: (spelling) C-A-N-N-O-N.

H E R B E R T S. C A N N O N, called as a witness on behalf of the petitioners, having been duly sworn, took the stand, was examined and testified as follows:

DIRECT EXAMINATION
BY MR. GELFAND:

Q Mr. Cannon, the parties have stipulated to your qualifications and experience and we'll put the same question -- briefly could you summarize the procedures you used in determining what the Class B common stock of Modern Maid Food Products Inc. would have sold for in August and September of 1968, under the facts -- existing at that time.

A Well I took a general overview first of the company, examined its operation and its history to date. I evaluated the investment climate at that time, uh, what asset values were, and what discounts might be applied; the, uh, type of security; its lack of marketability; it's, uh, lack of exercising control even though it was a substantial portion of the overall equities outstanding; its lack of dividend; the

limited growth of the company at that time over the past 3 years or 4 years; uh,what possibilities might exist principally for a purchaser or a group of purchasers to derive a profit from buying this stock and why would they get involved in the first place. In other words, could they force or seek or look to management to go public to sell out to somebody else, to merge with a public vehicle, to liquidate the business and retire, and what values might come up, uh, if they took any or all of those approaches. The general age of the principles, the sibling factor in the company, uh, also the amount of money that might be required to take a position in the company, uh, the cost of that money to the investor, and the time parameters pursuant to which he might be able to either retrieve the money and a profit and what would induce him to look towards getting that profit.

I looked also at underwriting conditions at that time. Uh, the, as I said again, the price earnings ratio or the value of the stock. I took a discount of the value of the preferred stock and its return to come up with a gross value for the common -- for the non-voting common. I then considered the liquidity factors under the existing securities regulations at that time and, namely, Rule 154, and the ability even if it did go public and even if its class was changed, none of which were factors at the time, uh, how long it would take to liquidate under the so-called

1% rule at that time where you could only sell a limited amount of shares every six months and then not on a regular basis. The fact that it had no rights of registration and that the company could never force any had it gone public. Uh, I considered the prices that I have been involved with in private companies and public companies for paying for stocks, not necessarily similar industries, although I had some involvement with this industry and with, uh, a company similar to it, and how much discount which -- and what profit potential you would have to minimally look for. Uh, the number that I used is that you must make within a 3 year period of time, 4 times on your money, or at least hope to make or you shouldn't get involved with an investment to begin with. And in doing that, you have to anticipate an actual ability to liquidate at whatever price. In this case there was no factual, at that time, ability to liquidate. Where I talk about a 4 times profit on your money within 3 years is where there might be defi -- there would be definite rights of registration, or a definite sell out, or a definite contractural obligation by the company to pur -- repurchase this stock in the event they don't do any of the other things.

Uh, in putting all those together, I would come out with a very nominal value that I might, as a speculative investor pay for it with the hopes of pushing management

towards doing something, and a value of about $2 a share, which is a very substantial discount from book. If I could assume that management would be very cooperative and that I would be able to liquidate within the 3 year period of time, I came out with a value between $5 and $6.50 a share. Uh, in my opinion, any price above that would be a, an extremely whimsical and speculative investor -- investment for an investor to make. And I personally wouldn't advise a client to do it.

Q Mr. Cannon, referring to your report, I wonder if you could clarify a little more what is -- you intend on the bottom of page 6 and the top of page 7 when you state, what must be emphasized here is the purchaser of a Class B common stock, non-voting, without the ability to force management to change the status of the stock from non-voting common to voting common could entertain no probability of ever liquidating the stock in the public market. Due to different class status none of the rules of the S.E.C. or ~~any~~ N.A., S.D. -- is that the National Association of Security Dealers?

A Correct.

Q Permit an automatic registration, even after a substantial holding period, to enable even piecemeal liquidation to the public -- into the public market. I wonder if you could clarify what these rules are, why if you have

a company that is already public that these shares couldn't have been sold, even on a piecemeal basis. I wonder if you could explain that.

A Well, that takes into consideration two situations. If you own non-voting or a separate class of stock and that stock has not been registered for public sale, you can't put it out until it is registered into the public market without the company cooperating and going through a registration for you. So you have a total lack of liquidity in the open market and you could only dispose of it under an investment letter and a private sale. If the company -- if you had a class of stock that was equal to the other classes of stock that were public, then you could only liquidate in the public market if there was a registration, whether it be what we call "shelf" meaning you've got six to nine months to liquidate it in the open market, or whether done through an underwriter at a fixed price, or agree to a price, or during 1968 you could liquidate under 154 no more than 1% of the total capitalization outstanding during any six month given period of time with the further -- further carry out being in the law that you could not do that on a regular basis that every six months you sell 1%. In this case there was -- after the recapitalization there's a million shares outstanding, they could sell 10,000 shares every six months, but if you did it for more than a year

and a half or two years, and you sold more than 30 or 40,000 shares that way, the S.E.C. very likely would come in and tell you, hold up for a couple of years and don't do it again, because it can't be part of a regular pattern. That law has since been changed recently into what the new 144 regulation that does permit a 1% liquidation on a regular basis every six months. And you can go on infinitum until you liquidate your total position.

Q A hundred years.

A If you own that much stock.

Q Oh, it's 1% of the total capitalization of the company, is that --

A Right. And that's further restricted by the -- in some ways by trading volume, if it's listed on a national exchange. So it could be even less than 1% in some circumstances.

Q This procedure of, you say an investor seeking 400% profit or $5 back for each dollar invested -- in your experience do these situations actuall prevail during the year '68? In other words, I understand from your --

A It's very common.

Q History, you were active in that and I was just wondering whether you knew of any?

A Yes, I was active as a stock broker and running a brokerage firm and more specifically running its corporate

finance department. And we, uh, had put together and did several private placements with that anticipation and in many cases with that realization.

Q Your value of $2 is based -- I'm reading this -- is based upon the fact that it would require -- because of the number of shares it would have required a tremendous amount of dollars to put in which would restrict the number of buyers?

A No, that's only one phase of it. The, the fact you would have invested close to $200,000 or $180,000 or $190,000 without any return, but more important without any chance other than making a total nuisance of yourself some how to force management to take you out, or somebody to take you out, or hoping to find, uh, in the hey days of '68 where everybody had a lot of loose money, of finding another investor who you could sell it to under an investment letter. Now these possibilities have kind of limited it. I, I've seen cases where somebody has owned over 51% of the stock of a company and couldn't force themselves on the board, after spending hundreds of thousands in legal fees. So, you'd have to just say that you're going to go in and either be friendly with management somehow and, uh, or have a heck of a lot of extra cash and say I'll wait out 5 years, 2 years, 10 years, whatever it takes until they liq -- eventually liquidate this business and try and make a profit. In that

case you've got to make more than 4 times on your money because your possibilities are extremely limited. And as a practical person, I wouldn't put a couple hundred thousand dollars in something that I couldn't have at least a, a definite probability of coming out whole within a 3 year period of time.

Q In other words you're -- But you feel that there would be always somebody who would put something in --

A There's always somebody and, and at $2 it's probably a good rank speculation and I might've recommended it to somebody if, if they were akin in the industry and thought that they could, you know, back door themselves together or had some in -- some other interests in it.

Q Now, assuming, you mentioned something about coming out whole or liquid in two or three years time, uh, then the value would be, is that $5 or $6, is that what you're saying?

A Yes, sir.

MR. GELFAND: I have no further questions. Oh, wait, I'm sorry, Your Honor. I forget sometimes. I did it twice today.

BY MR. GELFAND: (Resuming)

Q Is this -- Mr. Cannon, is that a copy of your report that you based your appraisal on?

A Yes, sir, it is.

In other words --

THE WITNESS: Substantially the same, yes.

THE COURT: 49% of voting stock in a, a --

THE WITNESS: It's almost as useless --

THE COURT: In a corporation where the other 51% is owned by someone else is, is subject to the same inhibitions as this. Is that --

THE WITNESS. Basically, yes, sir.

THE COURT: All right. Now isn't it true though in a, in a -- this was a New York corporation that -- that under those, those circumstances the, the owners of the majority control of the voting stock owe certain obligations to the minority interest?

THE WITNESS: Well to the extent that any, uh, Director or officer or majority holder owes it to his minority shareholders. In other words they can't go out and declare themselves million dollar salaries, just so nothing would be left, they couldn't just give away the net assets of the company, or any minority shareholder could come in and take action to stop them. That's what I meant when I referred to creating a nuisance of themselves to try and force them to, uh, liquidate a position for a profit.

THE COURT: Well aren't there people who have done this with considerable success?

THE WITNESS: Absolutely. Some people thrive on it.

The Court: So one of those might pay a considerable amount more than $2 for this stock, wouldn't he?

THE WITNESS: I sincerely doubt it. Uh, they would want to, in that case, make at least a 10 to 20 times profit based on marketability because they have to couple that with the fact that they are either usually attorneys and can do it themselves or have to hire attorneys at considerable expense to get the job done. And, and that's all time consuming and expensive and they generally will have a little more patience and very often can wait 5 to 7 years before they see a return. So, I doubt that they'd pay much more than 2, if that. Two is certainly what I think.

THE COURT: Mr. Goldberg.

BY MR. GOLDBER: (Resuming)

Q Mr. Cannon, how was the stock market in 1968?

A Sensational.

Q Sensational. How were new issues coming out?

A Cheaper by the dozen. They were coming out, uh, quite furiously and at very high PE ratios.

Q In other words, 40, 50,60 times earnings is --

A Well, no, the ones you read about that way -- most of the companies that have no earnings and no history of earnings, if you're going to compare it to a company that's been in existence for a while --

Q Right.

wouldn't sell to me for $2 a share.

Q So in other words, your $2 a share is strictly on what you personnaly would buy it for.

A It's what I think a buyer in, uh, in that class would pay for it. That's correct.

Q I see. Uh, so in other words, you've given the stock, the Class, uh, B non-voting stock approximately about a 95% discount?

A Off of book?

Q Off of -- no, off of your value of $33.70, if it was public?

A Under that set of circumstances, yes.

Q Or, but just for the fact that it was non-voting?

A No.

Q Not, not --

A Not just for the fact it was non-voting.

Q It was non-voting and, and it, it -- you say if it was public, it would be worth $33.70 a share, right? If it was marketable?

A No. If it was fully marketable, at that time, uh, yes. I guess that's what I came up with.

Q Right. In other words your discount is based on the fact that it wasn't marketable and it was a Class B stock? Non-voting.

A And had no ability to become marketable and a

Class A stock.

Q Well, yeah, but see you make a statement here, for public offering or merger with a public entity could not be reasonably expected within a three year period, and I would be loathe to invest more than $2. Now suppose it was reasonably expected it would go public?

A I would pay more than $2.

Q How much would you pay?

A As I came up to my price, at between $5 and $6.50 a share.

Q Did you know the following year this same class of stock, after it had been capitalized, was sold for $78 a share?

A That's correct.

Q And you still would only pay $6 six for it?

A I wouldn't have paid what the underwriter paid for it at the time it went public, personally.

Q You were associated --

A As an underwriter.

Q What -- you were asssociated with, uh, at one time with Weis, uh, Voisin, Cannon?

A Weis, Voisin & Cannon. I was president. Yes.

Q What happened with that company? Is it still in existence?

A No. I retired in '69 and it, uh, folded in 1972,

the end of '72.

Q So, based on your experience, uh, someone would expect at least a 400% return within a three year period at this time?

A Yes, sir, on private placements.

Q Uh, Did you ever recom -- recommend any investments that returned that high?

A Yes, sir.

Q A number of them?

A Several.

Q By several, how many do you mean?

A I can list them. Uh, I would put it to you this way, any one that we ever did in the form of a private placement, we expected at least that return, or we would not have done it.

Q Well, were you ever satisfied, that you did get 400%

A Oh, yes. I've got, uh, 1400% and, uh, more on occasion.

Q On occasion, but I mean for a company like this, what would you expect to return? Would a --

A For a company like this, as I said, I would expect at least a 400% return.

Q Wasn't that sort of unrealistic?

A Not at all. I think if you tie up money and you're

locked up and you can't quickly get out, and that's with an anticipation that you have an ability to get out; in other words, when we do a private placement we have a right of registration at the company's expense. So that the company between the 24th and 36th month must register stock for us, or we'll have an, a built-in ability to sell it back to them. And based on its road, or rate of growth, during that interim period of time and what it's done with the money we've put into the company, uh, we project out our return. It doesn't always happen. Uh, on 11, I believe, private placements I did while President of Weis, we broke even twice; we, uh, made 200% on the money within two years on three occasions; and we made better than 400% on the rest.

Q Uh, do you know that the 196 -- are you aware that in 1969 in June, there was a recapitalization?

A Yes, sir.

Q And all these shares became one class?

A Yes, sir.

Q And there would be no distinction in voting?

A Yes, sir.

Q And they'd all be the same class of shares?

A That's correct.

Q Uh, would that have had the effect on your --

A Absolutely. Uh, if it was all one class of stock

identification.

MR. GELFAND: Your Honor, may I call Mr. Silverman back for two questions?

THE COURT: Certainly. Certainly.

MR. GELFAND: To, to clarify something. Jack, will you take the stand.

MR. SILVERMAN: Thank you.

MR. GELFAND: He's unaware. I haven't spoken to him. It may be bad policy.

THE COURT: You've been sworn now Mr. Silverman just take a seat there.

MR. SILVERMAN: Thank you.

FURTHER REDIRECT EXAMINATION

BY MR. GELFAND:

Q Mr. Silverman, since December 31st, 1967, has Modern Maid Food Products Inc. paid any dividends on its common stock?

A To the best of my knowledge and belief, I don't believe so.

THE COURT: Maybe we'll aver another case.

BY MR. GELFAND: (Resuming)

Q Maybe the time is a question, we have stipulated that none -- no common stock dividends were paid in 1968. Were there any common stock dividends paid after 1968?

A No.

Q Okay. Thought the year might throw him. The -- I don't know if you've had time to think it over, but did the stock that was subject to gift, was there any repurchase, buy out, or buy back agreement with respect to the stock that was given to the trusts?

A No.

MR. GELFAND: That's all, Your Honor.

THE COURT: Thank you, Mr. Silverman. The Court had marked as Respondent's Exhibit O, a valuation report prepared for the respondent by the Manufacturers' Appraisal Company and it's noted that -- there the report concludes that the value of the stock as of the basic date was at $25 a share. Is that right?

MR. GOLDBERG: Your Honor, did I hear you say the Court concludes?

THE COURT: I, excuse me, I mean the report. The report I said, the report concludes that it was $25. Is that right, Mr. Goldberg?

MR. GOLDBERG: That's right, Your Honor.

THE COURT: So, uh, we -- and I, I don't recall any valuation case where the Court found a lower value than the petitioner's highest witness, but I'll, I'll look for that. So, aren't we -- aren't we somewhere within a range now of between $12 and $25, Mr. Gelfand?

MR. GELFAND: No, sir. In a --

Carter I think it was.

Q That's the United States District Court of the Southern District of New York?

A Yes, that's correct.

Q Mr. MacMullan, would you briefly describe -- well, Mr. MacMullan, what is the value of the stock of Modern Maid Food Products on the critical gift date, that you arrived at?

A It is my opinion that the value of the stock is best expressed as $25.00 a share.

Q And, how did you arrive at your valuation?

A I think it would be best if I very briefly ran through the appraisal report itself, I won't dwell in great detail on the pages since it is there in writing to be read, but if we would turn first to page 27, which is actually the first page that begins the valuation, I have taken three approaches to value, one of which I feel is more pertinent than others. But, the first approach here is a return on net worth approach, which simply compares the return that the subject company was making on its net worth, to the return that several -- five in fact, comparable companies were making in their net worth, an excess return is apparent, and that is capitalized at an intangible rate of return to determine the total value of the company.

The total value of the company based on that

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approach, the value is $5,200,000.00.

MR. GELFAND: Your Honor, may I please have a voir dire on the witness's qualifications, there are a few points I think that should be clarified?

THE COURT: All right.

VOIR DIRE EXAMINATION BY

MR. GELFAND:

Q Mr. MacMullan, in looking at Exhibit O, it is apparent that most of your activity, almost all of it, has been in the field of appraisal in real estate. You do mention that you have appraised stock in closely held corporations, can you please describe the nature, the activity of those stocks, were they real estate corporations?

A No, they are not real estate corporations. I think that the qualification sheet that you see there is somewhat misleading in that the large quantity of the items on there relate to real estate, however, for the past six years my primary employment for the Manufacturers Appraisal Company has been the valuation of intangible assets, including the stock in closely held corporations.

Q Well, what I am trying to find out is what is the activity of the closely held corporations, were the closely held corporations principally real estate corporations?

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A No, they are principally not real estate corporations, and they have run the full gamut of --

Q Could you give me a few of the names, just a few of them, please?

A I could give you a detailed list of 15 or 20 of them, if you would like, I don't have them with me.

Q Well, would you know the names of three of them, and what fields they were in?

A I'm not sure, let me think. Well, let's see, Smith Lumber and Supply Company, they retailed lumber supplies. And, quite frankly I'm stuck for the names of -- of these companies, I would be happy to give you a full list of every company that I have appraised in the last 2 years, and you will find that, you know, they run the complete gamut of different types of industries, and so forth.

Q Have you had any actual experience in counselling purchases of securities of closely held companies?

A Not in the purchase of them, I would say yes in the sale of them. One of the reasons that people want appraisals for the stock in closely held corporations is to decide what they should sell it for. They may be considering going public, they may be preparing a trust of some kind, or they may be preparing -- you know, for a personal estate. And, they come to us frequently and ask

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mony of my witness.

THE COURT: You may, you may.

DIRECT EXAMINATION BY

MR. GOLDBERG: (Resuming)

Q Mr. MacMullan, have you -- do you remember where you left off?

A Yes.

Q Okay, would you please pick up again?

A I would like to go to the second approach that I took, which is a price earnings ratio approach, and it is on page 29 it starts.

It simply compares the price earnings ratio of five comparable publically held companies to the -- and applies that ratio to the earnings of the subject company for the year ending December 31st, 1967. That produces a total value which is then discounted for lack of marketability that discount being determined by the actual cost of location of a common stock issue of that size.

Skipping over to the next approach, is a comparable public enterprise approach we call, it, it begins on page 32, and that is really quite similar to the price-earnings ratio approach, except that it considers two other factors as providing some evidence of value, and that includes net worth and sales, in addition to earnings, and develops multipliers and applies them to the subject company's earnings,

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net worth and sales, and once again, discounts the total value of the company so determined by an 8 percent amount estimated to make the stock public.

So, at that point we have run through three approaches and it was my opinion that the last one, the comparable public enterprise approach provided the best insight into the value, and that the $7,000,000.00 figure was the best estimate of the total value of the subject company.

We then reduced this in value, in an attempt to determine the value of the class B common stock, we subtracted off first the value of the preferred stock, the cummulative 5 percent non-voting preferred stock, and I used the $100.00 redemption value, even though I realized that the amount of interest that that stock would -- the 5 percent interest was somewhat below market, and that stock would probably actually have sold on the open market for something like, oh, $75.00 or $80.00 a share.

But, I used the full amount because in fact it was redeemed a year later, and perhaps there was some indication that that might have taken -- was going to take place. Anyway I subtracted off the value of the preferred stock, that's $2,520,000.00, and leaving a residual value to all the common stock, both class A and class B, of $4,480,000.00. Strictly mathematical division of this total

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value by the total numbers of class A and class B shares produces a total value per share of $40.00.

However, we realize that the class B is both a minority interest, or rather the subject stock is both a minority interest and it is class B non-voting, so there is some further discounts to be taken into consideration.

I've used 25 percent as the best indication of the proper discount for the minority interest, and there is a study of two step acquisitions contained in the addendum of this report, which is my basis for utilization of the 25 percent. An additional reduction in value from -- at this point we are at $30.00 a share, and I've taken off another $5.00 a share for the fact that it is non-voting. I'm not really sure whether this is correct, since the elements that are missing for both non-voting -- for both the class B and the minority interests are the same thing, that's a lack of control, but at any rate, I guess there really is something to be said for the fact that the class B minority interest is worth less than a class A minority interest, because the potential for control doesn't exist with the class B, you can't form any kind of a combination with anyone else, and get control of the company, so I've taken a $5.00 per share discount, or a reduction in value from that, and that is how I got the $25.00 a share.

I think that -- that there is two points that I

would like to go into in some detail, and I know that you probably will want to talk to me about it on cross examination anyway. And, I really feel that the comparables that I used I must talk about those and explain why I used them, and I do want to go into a little bit more detail about the discounts taken.

I readily admit that the comparables are really not comparable to the subject company. We found in fact no companies that were really comparable. And, nevertheless though, I feel that -- that the five companies that we did select are useful, and that they can be helpful in estimating value. And, maybe if I go over some of my reasoning it will become clearer.

I had available to me the Prospectus, which is dated October 28th, 1969, and on both page 3 and page 6, it outlines what the subject company did, and it explains that they manufactured breading and batter mixes prepared to customer specifications for food processers, and that they also manufactured fully prepared flour mixes that required the addition of water before baking for use in restaurants, hotels, hospitals, and other institutional mass feeding outlets.

And, it also outlines that breading and batter mixes for 1967 constituted 55 percent of the sales of the subject company, and that prepared flour mixes constituted

approximately 43 percent of the sales for that year, 1967.

And, also on page 7 it mentions that the principal raw material that the subject company used was wheat flour.

Now, we already -- the study that we made, we found that there was really no companies that made, at least no comparable publically held companies that made breading and batter mixes, that were in the size range of the comparable, of the subject company. And, so we know right away that 55 percent of the company's business is really not comparable to that of a listed company.

So, we are down to looking for companies that make prepared flour mixes, or perhaps that have wheat flour as a principal raw material, or who might be selling to similar customers. We are looking for sort of second echelon comparables here, for something that is comparable, secondary,or an indirect way, but which might still be of some use, or some help to us in determining value.

Another factor that I felt was important was to find comparables that are roughly in the same size. I realize that Phillsbury,General Mills and DCA Industries are competitors of the subject company, or were competitors of the subject company, but I felt that they were so large that -- that -- and they were into so many diverse fields, that to make comparisons with those companies is really not

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meaningful.

Now, in the addendum of my report between pages 37 and 43 --

MR. GELFAND: Your Honor, I think that it is apparent from the witness's testimony and from examination of pages 37, 38, 39, 40, 41, 42, and 43, dealing with his comparatives, that they are, with the exception of Martha White which may overlap a little bit and I think that the witness will bear out that what they sold was in the retail field, there isn't any one that even approaches what the taxpayer does, and it isn't a question of using it as a guide, but what he did was actually take their figures and statistically apply it to our taxpayer, and I therefore say that this whole report is based on facts that are completely foreign and irrelevant to our situation, and I move that the report be striken.

THE COURT: Your motion will be overruled. I think, Mr. Gelfand, that this all goes to the weight to be given to the witness's testimony.

MR. GELFAND: But, they are -- all right, we'll do it on cross, Your Honor.

THE COURT: Because -- I think actually this isn't the first time that we have had to determine the fair market value of a company with respect to which there are no comparables, public listed securities to use as a guide. Now,

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that's done all the time, and the witnesses can make all kinds of approach to that, and when you get down to deciding as to whether or not you are going to accept their conclusions, why you look and see whether their approach makes any sense, that's all, isn't that right?

MR .GELFAND: Your Honor, I can understand as a guide to get some general feel, but this witness has done more than that, he has taken their figures, and interpolated them against the actual --

THE COURT: Well, that the Court will take into consideration. And, I would assume for example that Mr. Silverman could probably successfully do what Martha White does, if he put his mind to it. And, I would suspect that they probably put the same thing basically that he sells in a cardboard box and it goes on the grocery shelf, now the formulation may be different, but they have obviously an acceptance or a trade name, or a tie in with Safeway, or something that enables them to sell that way.

BY MR .GOLDBERG: (Resuming)

Q If you would continue, Mr. MacMullan?

A Certainly. I was going to mention that between pages 37 and 43 of the report, are outlines of the comparable public enterprises that we used, and there is a brief summary of the business -- the type of business that those companies do.

I feel -- I admit that they are not comparables, however, frequently this is a problem that we have when we are faced with making a valuation of -- of stock in a closely held corporation. Frequently there are no comparable publically held companies, so we do the best that we can.

I don't think that the -- that the -- the earings multiple for example of 14 that I utilized is necessarily high or necessarily incorrect, and I offer this next statement only in a confirmatory way, it -- it didn't contribute to my utilization of the 14 multiplier, but I note that in 1969, the $12.00 a share public price, is about 14.4 times the 1968 earnings. So, it is not necessarily wrong. And, I didn't - - I didn't use that 14.4, in fact I really didn't become aware of it until I had developed by own figures, but I do offer it in the way of confirmation of the reasonability of the answers that we did get from utilizing these comparables.

The next subject that I would like to just briefly touch on is the discounts that we used. We used three basic discounts, one for lack of marketability, of 8 percent, one for the fact that the stock was a minority interest of 25 percent, and one for the fact that the stock was class B non-voting stock of $5.00, which if expressed as a percentage would be about 16 2/3rds percent.

I think that the total discount taken is -- is

reasonable, and -- and I enclose in the addendum of the report starting on page 44 some Court cases that touch on the discounts for fair market value from stocks, in closely held corporations, and I don't think that any of these total over 50 percent, and if you read through the cases you will see that some of those that are up about 50 percent had much less to offer than the subject company in the way of future possibilities.

I think that that ends my basic testimony.

Q Mr. MacMullan, so you have stated, am I correct, that you used these "comparable companies", as a mere guideline for in your best judgment the -- the only companies that you possibly could compare them with in size and sales and product line?

A Yes, I feel that in an instance like this you are faced with two alternatives, one taking an arbitrary price earnings multiple of some kind, and ten seems to be the standard one when somebody wants to get arbitrary, they generally take ten, or attempting to make some comparisons with companies that have some things in common with the subject, and that's the route that I chose.

MR. GOLDBLRG: No further questions.

THE COURT: Well, let me ask the witness, isn't it true though, and looking also at the report of the gentlemen from the American Appriasal Company, and I doubt

remark on their most closely related, and then they were because they couldn't find anything else, he didn't take those figures and apply them, he said based on this, these are what these established companies with good will, name, good will in the marketplace, good will on their product, their diversification, their economic clout, if they sell at this multiple, what should this small little, unknown company sell for. And, then he said maximum ten times.

But, in this particular case as we review this, the witness hasn't done that.

CROSS EXAMINATION BY

MR. GELFAND:

Q Mr. MacMullan, would you say that investors divide roughly into two categories conservative and speculative?

A No, I wouldn't say that.

Q Well, into what categories would you divide the investors?

A I would say that they are probably the two extremes, and people fall into all kinds of classifications in between.

Q I know, but I said roughly those two categories, and then there of course are those in between?

A You asked me if I would say that, and no I wouldn't say that.

Q All right, what categories would you say they fall into?

A I wouldn't try to number a certain number of categories that investors fall into.

Q No, I'm not trying to get a number --

MR. GOLDBERG: Your Honor.

BY MR. GELFAND: (Resuming)

Q But what raw groupings do they fall into?

MR. GOLDBERG: I think that this is meaningless, because you can have a buyer for any kind of business, it all depends on the price, the business, the questions --

THE COURT: Well, I -- let Mr. Gelfand pursue this a minute.

BY MR. GELFAND: (Resuming)

Q Would you disagree with this statement, Mr. MacMullan, a fairly conservative investor who purchased for an investment is concerned with his powers of control, the liquidity of his investment, the opportunity to revamp the asset holdings of the company, his net return by the way of dividends, as compared with other opportunities in the open market?

A Are you asking me if I would disagree with that?

Q Would you agree with that or disagree with it?

A I would not disagree with that.

Q Then what do you believe are the criteria that

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a speculative investor uses?

A I would say that a speculative investor, while he may consider those factors that you mentioned is more concerned with the immediate return or short term capital gain of some kind, something like that.

Q In other words he will just weigh the risk out of how much he will get out of it within a relatively short period of time?

A Would you say that again, please?

Q He'll weigh the risk of loss against what his possible gain would be, and the cost of carrying it if he should happen to be locked in, even a speculative investor would consider what's going to happen if I'm locked in wouldn't he?

A Yes, but you haven't said anything that's different from a conservative investor, and --

Q Except he is willing to take more of a risk.

MR. GOLDBERG: Your Honor, Mr. Gelfand is sort of arguing back and forth with the witness.

MR. GELFAND: No, I am trying to find out what criteria a speculative investor uses, or any investor.

MR. GOLDBERG: I think that we are getting far afield --

MR. GELFAND: Well, if --

MR. GOLDBERG: In the questioning, Your Honor.

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THE COURT: I think that the Respondent's objection is well taken in that you have all types of investors.

BY MR. GELFAND: (Resuming)

Q Would you say any investor is concerned about the length of time that he might have to make his investment in a situation?

A Yes.

Q Is degree of risk of loss against -- weighed against the possible gain?

A Are we -- which investor are we talking about?

Q Any investor is concerned with his possible risk in going into a situation, and his possible gain that he may get from a situation?

A Certainly.

Q The possibility of liquidation?

A I would say that that is a factor.

Q The available market in which to dispose of the stocks subsequently?

A Yes, I already answered in the affirmative to this with your other --

Q All right, what criteria does an appraiser use a general rule in selecting comparable companies?

A He attempts to find companies that are comparable in as many areas as possible.

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Q Size would be one?

A Size would certainly be one.

Q Product?

A Product, right.

Q The market whether it is retail, wholesale or manufacturer?

A Customers.

Q The customers that you are selling to, trade name, length of time that the company has been on the market?

A No, this would be an ideal comparable.

Q I mean these are the factors --

A Which practically never exist, but yes, you certainly love to find five that were that way.

Q All right, let us turn to your comparables please.

MR. GELFAND: Pardon me, Your Honor, I can't read --

(Pause.)

BY MR. GELFAND: (Resuming)

Q Now, let's turn to page 43, Spaulding Bakeries, Inc.

A 43?

Q Page 43. Now, what does this company do?

A You are asking me what it does?

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Q Yes.

A It operates a bakery, selling bread, rolls and crullers in New York, Connecticut and Pennsylvania, under the name County Squire.

Q It it one bakery?

A I don't know, I would assume that it does not have one bakery, since it is listed as being in three States, it must have more than one bakery.

Q All right. And, what does it sell, to stores, does it have its own stores, do you know, does it sell to other stores?

A I don't know.

MR. GOLDBERG: Your Honor, this is -- Mr. Gelfand is going over the comparables, the witness has testified that these are not comparable to the subject company. The Court realizes that these are not comparable to the subject company exactly, and it is his best estimate, his best judgment to use certain criteria in comparing similar companies in the sense of size and maybe the product lines, in the bakery business the same way that --

THE COURT: Well, let me ---let me ask the witness, where did you get your information as to these five companies, off of those yellow what are they Dunn and Bradstreet sheets?

THE WITNESS: No, these are from Moody's Industrial

Manuals.

THE COURT: Moody's sheets, right.

THE WITNESS: From the actual bound manuals.

THE COURT: Yes, they are from the bound manuals, so that the only information that you know about these companies is the information that you got from Moody's, is that right?

THE WITNESS: That's correct.

THE COURT: Okay. That short cuts that.

BY MR. GELFAND: (Resuming)

Q Would you say that Saps Foods Inc. is any way related to what the Petitioner in this case does?

A Yes, I would say in some way it is related.

Q In what respect?

A Well, probably their primary raw material is probably -- is probably flour, wheat flour, so they have -- they are buying the same product, they are buying the same raw material as the subject company.

Q Well, does a bagel manufacturer use wheat, or a pretzel manufacturer, would you say therefore a pretzel manufacturer or a bagel manufacturer is similar to this taxpayer?

A I --

Q Even somewhat closely related? Is the operation of three restaurants, and the sale of things through vending

machines similar to this -- to what this taxpayer does?

A No, it is not.

Q Or even closely similar?

A No, each one of these comparables had some things that they do that are really not comparable at all to the -- to the subject --

Q Well, what does Sap's Foods do except use -- possibly use wheat, that is similar to what this taxpayer does? By this taxpayer, I mean Modern Maid Food Products, Inc. I'm waiting for an answer, I sat here waiting.

A Well, you asked me to express an area of comparability and I did express that as being the utilization of the same raw material, to me that is an area of comparability.

Q All right, let's take Bridgeford Foods, according to your record here, they distribute, manufacture, wholesale distribution of processed meats and delicatessen foods, that's their principal item. How was that related to what this taxpayer does, except that it is food?

A Of course, you only read part of the --

Q All right, the sale of fresh frozen smoked meats, and then as the fourth item, which I assume is listed in order of importance, the manufacture and sale of frozen bread dough products?

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A Right, that of course is the area that has some comparability.

Q And to whom -- do you know to whom the frozen bread dough products are sold?

A No, I don't. We have already established that -- you know what I know about these comparables by reading the business thing.

Q The Manischewitz or Manischewitz, I have heard both pronunciations, on page 39 --

A Um-huh.

Q I guess they use wheat and matzos, matzo meal, farfel, cake meal, tam tam crackers, then we go to a little bit of different field, borscht, gafilte fish, baby foods, canned soups, Kosher sacremental wine, candies, and so forth. You mean the making of matzos, which is sold on the -- trucked to the stores for retail sale, that is the close relationship or the similarity with something that Modern Maid Food Products does?

A Well, it certainly is not a close relationship, I haven't pretended that it is. But, once again we have a similar raw material. Are we going to talk about Martha White Foods too?

Q Would you know how much the -- though you may have it, I don't know how much the net income sales from each phase of each activity of these companies I referred

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A No, I don't.

Q Turning to your valuation on page 27, return on the net worth approach --

A Um-huh.

Q Assume the last earnings in balance sheet figures known are the close of a previous year, wouldn't a perspective purchaser be obliged to use those figures? In other words you have on page 27, the 1967 figures, and then you refer --

A Right.

Q On page 28 to 1968 figures, or using them as a guide, now assume for the moment, you don't know, though the testimony is that way in the Court, that there were no interim figures taken off, that the audit is made once a year, and the 1968 figures are known sometime in 1969. And, you have a prospective purchaser on August 21st, 1968, would he know any more than the figures of December 31st, 1967?

A No, of course not.

Q Then, in making an appraisal wouldn't you more or less have to use those figures, if the figures after that date are not known?

A If you are following your assumption, yes, that's right.

Q Only on my assumption, fine. Now, when one makes

a purchase, do you only look at securities stock of a closely held company, or any security, does one only look at the last year's earnings, or do they look at the year before and the year before, you know at least three years' earnings?

A Well, certainly they would look at as many prior year's earnings as they would have.

Q All right. And, wouldn't they be concerned to see if in those three years the earings were flat or the earnings showed an increasing trend?

A Yes, they would be.

Q And, it would be reflected in the market price, certainly, as a growth situation or a flat situation?

A Yes, that's right.

Q Mr. MacMullan, on page 30 of your report you have a series of rotations, number and size of rotation, number of rotations, and the cost of rotations, which is how you arrived at an 8 percent discount for going public. May I ask you where you obtained these figures?

A Yes, this was information that was made public by the Securities and Exchange Commission.

Q For 1968?

A No, I believe in fact these are considerably before 1968, prior to 1968, it would have been available to someone in 1968, however.

Q Well, are they 1967's?

A I'm really not sure, you know what year this relates to.

Q In other words this could relate to some year that has no bearing at all on the cost of going public --

A Well --

Q Have you recognized that there is a -- do you recognize --

MR. GOLDBERG: Your Honor, that's -- that's three questions in one.

THE COURT: Wait a minute.

MR. GELFAND: I think that he answered the other one.

(Pause.)

MR. GELFAND: I -- may I -- I thought that the Court was doing some calculations, are you waiting for me, I was waiting for you, Your Honor?

THE COURT: Yes, no, I'm waiting for you, Mr. Gelfand.

MR. GELFAND: Oh, I'm sorry.

THE COURT: I'm waiting for you, I was just doodling, that time.

MR. GELFAND: I'm sorry, Your Honor. There was a question, and I heard wait a minute, and that's it. All right.

BY MR. GELFAND: (Resuming)

Q Going back to my questions, do you know what year those figures of the SEC refer to?

A No, I am not sure what year they refer to, I am sure that they are prior to 1968.

Q Do you know, can you name any one company the size of Modern Maid that went public in 1968 or 1969 at a cost of 8 percent?

A You mean other than Modern Maid Company?

Q Other than Modern Maid?

A No, I can't.

Q Now, in these costs, is this just the underwriter's cost?

A Yes, that's correct.

Q Now, let's see what other costs, are there usually legal fees?

A Yeah, there are legal fees.

Q Accounting fees, special accounting fees?

A Yes there are. The bulk of the costs, however is the underwriting fee.

Q And, sometimes underwriters in addition to their initial charge get warrants, or buy cheap stock?

A Sometimes.

Q Sometimes. So those are all additional costs?

A Yes, however you will note that -- that the range

of costs that were available to me by this summary was 6 to 8 percent, and I used the higher figure than the 8 percent figure, maybe that offsets some of those additional costs that you are talking about.

Q That gets us to another phase. When one goes public, when a company goes public, is every single share sold, or is there a registration of some shares and the remaining shares, and some shares remain restricted?

A It -- it depends on the offering, it can be done both ways, certainly.

Q Well, every single share that the insiders hold is being marketed and sold out, aren't they in effect selling their company and withdrawing from it?

A I don't --

MR. GOLDBERG: Your Honor, is that a question or a conclusion?

MR. GELFAND: NO, with a raised voice, that's a question.

BY MR. GELFAND: (Resuming)

Q If every single share is registered and sold by the underwriter, aren't the insiders then selling their company?

A They are selling their stock in the company, certainly.

Q Is that how you are appraising this, that Mr. Silverman was selling his interest in the company?

A No, I'm not appraising it that way.

Q All right, let return to page 27, on page 27, you have an average for percentage of return of earnings to net worth of 12.89 percent and you used 13.0 percent.

A That's not correct.

Q That's not correct? What is your average then?

A You didn't say average, you said you had a return of 12.89 percent.

Q I'm sorry -- I'm sorry, an average return, I'm sor[illegible]-

Yes.

Q An average return on the net worth of 12.89, percent which is rounded out --

A Yes, I must point out that I also had a composite return of 13.77 percent.

Q But the 12.89 percent is the lower rate of return, so therefore 13 percent was taken, right. Let's -- now in that 12.89 percent you have an extremely low one, 6.94 percent, and one quite a bit above the others of 17.53 percent, Martha White?

A That's correct, yes.

Q All right. Where such a wide disparity exists, isn't it customary to eliminate the high and the low items?

A It is not customary, it can be done, it is an approach to things.

Q May I refer you to page 29, did you in that case have an average without the high and the low, and you used that one?

A Yes, I did.

Q All right, let's go to page -- 50, you have an average of 31, and an average without the high and low of 24, and didn't you use the one close to the 24, of 25 percent, which you said was the basis for your 25 percent?

A Yes, I did in that case, I think that in that case the high and the low are so far out of line, it is called for.

Q Well, isn't 17.53 and 6.94 out of line, isn't the 6.94 certainly out of line with the others?

A We are back on what, page 27?

Q Page 27.

(Pause.)

A Yes, I feel that they are out of line, however I feel -- you know that there is similar indication of percentage that's indicated by the composite and the average is my basis for using 13.0 percent.

Q Well, wouldn't you have that effect if one of the companies was weighted in the use of the figures that

it was so much greater than in others, that one could tend to offset the other? Isn't that actually what happened here? That the weighting of Martha White because of its size compensated for the extremely low figure on Manischewitz Company, and therefore your composite was what you consider almost the same? Actually if you eliminted the high and low, wouldn't you be closer to the composite, if you are saying that you are using the composite as a guide?

MR. GOLDBERG: Your Honor, Mr. Galfand is in a narrative form asking so many questions in one, and it is just arguing with the witness as to the --

THE COURT: I think that most of what you are saying, Mr. Galfand, could be very well taken care of in your brief.

MR. GOLDBERG: It is purely argumentative, Your Honor. It goes to the weight of the report.

BY MR. GELFAND: (Resuming)

Q Mr. --

THE COURT: I think that any witness called upon to do this type of job, why he is pretty much entitled to use any approach that he wants to, and then the reasonableness of his approach will be taken into consideration in determining the weight to be given to his testimony.

BY MR .GELFAND: (Resuming)

Q Mr. MacMullan, have you made any calculations of what the figures would be on page 27 if you had used the composite percentage return?

A No, I haven't run through what those figures would be.

Q You said that you used 13 because it was pretty close to the composite, would you consider using the composite a fair basis too?

A No, obviously I feel that the 13 percent is -- is my estimate of a reasonable rate of return based on the comparables, and that's why I used it.

Q Why 13, in preference to 13.77?

A Because we have both -- we have two figures expressed here, 13.77 as a composite percentage return on net worth, and 12.89 as an average return -- percentage return on net worth, I used something in between the two, and it was actually closer to the average than it was the composite.

Q You did -- state that with respect to two other averaging you took the figures without the high and without the low?

A Yes, but neither of those did you have the opportunity to determine composite or average figures.

Q I believe that we have composite figures on page --

A I beg your pardon, I -- made an error in that, on page 29, you are looking for, there is a composite expression of the price earnings ratio.

Q Right.

A Of 17.9.

Q And, if we were -- all right, we'll pass on, leave it all for brief and calculation. On page 28, no page 29, I'm sorry, you have total value for each of your five selected companies, how did you determine these values?

A They were determined by a simple multiplication of the value of their shares times the total number of common shares outstanding.

Q And, is that listed on page --

A 33.

Q 33?

A Um-huh.

Q Now, this average price that you have listed, that's an average price of what?

A That's an average price of the stock for the year.

Q For the year?

A Yes.

Q You mean from January to December?

A Um-huh.

Q And, that's the figure that you take for August 31st -- August 21st to September 24th, on marketable securities?

A I believe so, let me just -- make sure that's what -- I have done here. Yes, that's what I have done because these -- these stocks were only traded in a limited manner, there is no way of determining the price of the stock on a given day, that far in the past, and they are not listed even in our over the counter exchange for example.

Q Well, let's take Bridgeford Foods, do you know what the range was for the year?

A I don't know, is it in the comparable section of the report?

Q It is on page 33, that Bridgeport Foods, one of your selected companies -- that is in the business of selling processed meats and delicatessen foods. Do you know what its range was for the year?

A No, I don't. I did know when I made the calculations, I don't know now.

Q I --

A Actually, Bridgeford Foods was offered, I think, it went public on -- or had a public offering or issuance on December 19th, 1968, at 8 3/4 a shares, and that is the figure that I used for that particular company.

Q Well, may I ask you to turn to page 41? How many common shares were there of Bridgeford Foods on November 1st, 1968? Outstanding?

A 600,101 shares.

Q And, October 31st, 1969?

A 704,301.

Q Didn't you determine that there was a offering of 100,000 shares, and that 4200 shares went to the underwriter, and that there was a public company owed during the year, you didn't determine that?

A I'm really not sure what your question is.

Q I'm asking you when you took these figures that there was a public offering in December the 10th, 1969, didn't you verify that that was only a public offering for 100,000 shares? And, that the other 4200 shares was then given to the underwriter as part of his compensation?

A Yes, I was aware of the size of the offering.

Q It was 100,000 shares?

A Un-huh.

Q And, there were 600,000 shares previously outstanding?

A Yes.

Q And,you didn't go to check what the market price was of that stock during the year -- even take an average as you did on the others?

A Well, in this case I thought that we had something that was better than an average we had a price that it was actually sold for at or near the dates of -- the as of dates of this report.

Q December 10th, is near August 21st, all right?

A It is not near August 21st, it is near December though, which is another one of our dates.

Q August 21st is the date of the gift, pardon me, did you know what dates the gifts were made?

A Yes, I understood that there were several gift dates that we are talking about here.

Q What gift dates have we got at issue in this proceeding?

A We have some in August, and September.

Q That's right. Do you believe that list of publically traded stocks vary, the market price varies from August to December?

A Yes, certainly.

Q Now, if that figure instead of 8 3/4 was some other figure like 6 or 5 or even 4, that would change all of your ratios and everything else, wouldn't it?

A If -- if in December of 1968 they went public at a price of 6 or 5 or 4, it would change my ratios, yes.

Q No, I said if on August 21st, where the average for the year was 4 or 5 or 6, that would change your whole

table and all your percentages, wouldn't it?

A You misunderstand, I had an opportunity to use an average for the year for that company, and I chose not to do it because I felt that the 8 3/4 price as evidenced by its sale in December of 1968 was better than the average for the year, and that's --

Q May I ask you why you thought it was better than the average for the year? Why should a price -- even if the average for the year is correct, why didn't you get the average for August, or the average for September?

A Because I was unable to find for these companies, the small size that they were, prices -- sale prices as of the given date of this particular valuation problem.

Q Are these over the counter traded securities?

A They were not at the time, no. Martha White may have been, the others were not, they are traded -- they are registered with banks and things like that, traded that way.

Q Have you ever heard of the expression pink sheets?

A Yes, I have.

Q All right, aren't securities of a number of companies that -- what should I say, that are not actively traded, aren't they listed in the pink sheets, bids --

A Yes, let's put it this way, when I say that they

are not traded over the counter, I meant that they are not listed on the over the counter market, and therefore you can't find by reading -- you know, the over the counter market --

Q You can't pick up the New York Times, and find it, --

A Right, it is infrequently traded stock.

Q But, aren't there still means of determining the price at which stock are being traded if they are not listed in the New York Times or the Wall Street Journal as listed over the counter stocks?

A Yes.

Q Aren't there means of finding out --

A Yes, there certainly are.

Q But, you didn't even do that in this case?

A The more current that the stocks are, the more near you are talking to this date today, the easier it is to do.

MR. GELFAND: Your Honor, may we have the record held open so that I could show, present to the Court what Bridgeford Foods was selling for, and show the effect on it in August and September?

THE COURT: You mean on the pink sheets?

MR. GELFAND: Or from the National Quotation --

THE COURT: Because if you do --

MR. GELFAND: Service.

THE COURT: I think that maybe we will have to have evidence to show just how that pink sheet was made up, and how reliable it was too, Mr. Gelfand.

MR .GELFAND: Well, what about from the National Quotation Service? There is a listing put out by the National --

THE COURT: We've had case after case in this Court, Mr. Gelfand, where at this time a lot of these prices were made by people selling to each other, and the Court would be inclined to agree with the witness that when he had a reliable public offering that was a lot better than the pink sheet. The pink sheet may have reflected some transactions in preparation for the public offering, I don't know.

MR. GELFAND: What about the fact that the public offering that sometimes the market is raised up just for the public offering and then it sells down again?

THE COURT: I say it may very well have reflected some transactions.

MR. GELFAND: All right, it works both ways, Your Honor.

THE COURT: That's right.

MR. GELFAND: Off the record, may I tell Your Honor a brief story about this? Hold it off the record,

please.

THE COURT: We have only a few minutes left on the tape, we'll give you another five minutes, how's that?

BY MR. GELFAND: (Resuming)

Q On the other figures that you have, average price for the year, where did you get that information? It is not from the New York Times, the Wall Street Journal and they are not active, that way, didn't you take them from the pink sheets?

A I took them from Moody's, which gives you a list of --

Q Where does Moody's get it from?

A I don't know where he gets it from.

Q In other words you just took Moody's figure without knowing whether it is right, wrong or otherwise?

MR .GOLDBERG: Your Honor --

THE WITNESS: Yes.

MR. GOLDBERG: That's purely argumentative, I would hope that Moody's would print rather accurate information because so many people are relying on their investment service.

MR. GELFAND: But if there is no daily market for it, Your Honor,then Moody's have no place of getting it but the pink sheets, unless we call Moody's in to show it.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, would you say that the dividend the company pays is a factor in the price earnings ratio?

A In the price earnings ratio?

Q Yes, what you call your P.E. ratio, market value compared to earnings?

A I would say that it is a factor indirectly in that it is certainly something that someone who is buying the stock would consider.

Q Do you know what dividends these -- your selected companies paid in 1968?

A Well, -- when you get into the area of dividends and the valuation of closely held stock, it is my feeling that the dividends are essentially a function of earnings and of net worth, and if you are going to consider them again, you are doubling up and considering something twice.

Q On page 33, comparable public enterprise approach, didn't you take into consideration earnings, net worth, and sales as three separate factors?

A Yes, I did.

Q All right. Now, when you compare each one to the market price, or total value, which is the market price times the number of shares outstanding, aren't you in effect giving consideration to the fact that a stock

paying a dividend, may sell at somewhat more than a stock not paying a dividend?

THE COURT: I think that may be your conclusion, not the witness's.

MR. GOLDBERG: Right.

MR. GELFAND: No, I'm asking him if --

THE COURT: Counsel, I mean take Eastman Kodak, or IBM, or -- these high multiples don't pay any dividends, do they, these rich fellows, -- rich tax lawyers like to buy those?

MR. GELFAND: These -- these companies aren't Eastman Kodak, American Telephone, I'm not talking about that, Your Honor, but when --

BY MR. GELFAND: (Resuming)

Q Let me ask him, hasn't a dividend any effect on the price earnings ratio of a stock?

A Well, you asked me that question once, and I said I feel that it has an indirect value, I'm not really sure how it would be measured, but --

Q All right, then I asked you did you know what dividends your selected companies were paying in 1968?

A I had that information available at one time, I don't know right now what it is, no.

Q You didn't play any part in your determination of fair market value, though, did it?

A No, it did not.

Q Would you please -- all right, on page 33, you have Sap's Food, with an average market price of 8, and you have Spaulding Bakeries with an average price of 8 1/4. Is that correct?

A Yes.

Q All right. Now, would you turn to your financial statements on each one, Sap's Food, is on page 42.

THE COURT: I think that we are going to have to recess at this point, and let the Reporter put a new tape in, so we'll recess until 11:30.

THE CLERK: All rise, please.

(Whereupon, the hearing in the above was recessed at 11:20 as described above.)

Tape 16 gv

BY MR. GELFAND: (Resuming)

Q I had suggested, Mr. MacMullan, that you turn to page 42, which list the financial data with respect to Sap's Foods, Inc. Now, am I correct your figures show that for the year ending May 31, 1967, this company earned $.49 a share and the next year $.71 a share, and the year ending May 31, 1969, $.90 a share?

A That's correct.

Q And, this company did not pay any dividends?

A That's correct.

Q Now, if we turn to Spaulding Bakeries, you

have the earnings for two years here, Spaulding Bakeries earnings are $.81 in 1968, and $.77 in 1969. In other words the same relative figures, but Spaulding Bakeries was paying a dividend, if my computation is correct of $.52 a share. In other words $218,000.00 on 420,000 shares in 1968, and in 1969. Is that correct?

A Yes.

Q $.52. So, the lack of growth in Spaulding as compared to Sap's Food was compensated by the dividends that Spaulding was paying and Sap's Food wasn't paying, if the market price is the same?

A That's your conclusion.

Q Well, what do you think it is?

A I think that that may be one of the factors that kept the price in the same area.

Q As an appraiser, would you say that Sap's Food would be worth -- the stock would be worth no more even if it paid a dividend, it wouldn't be selling any higher?

A As I have expressed before, the -- the contributory element of value to -- the -- that the dividend plays is really difficult to measure, and I have regarded -- I have considered dividends in this report, but I considered earnings and net worth basically, once you consider them, you have in effect considered dividends.

Q You are taking -- if you were considering earnings

to net worth only, I recognize that is a measure of the dividends, is compensated for a little bit by the fact that the dividends has reduced the net worth. But, you are also taking earnings to market price, and therefore --

A Um-huh.

Q And, therefore if a dividend has any affect on market price, the fact that one stock is paying a dividend --

MR. GOLDBERG: Your Honor, I object to this, this is purely argumentative, and should be brought out on the brief.

THE COURT: Objection sustained.

MR GELFAND: All right.

BY MR. GELFAND: (Resuming)

Q Let us go to page 33. In this -- on this schedule you have your first -- well, the third column from the right, you list earnings as a percentage of total value, and the total value is the market price times the total number of shares outstanding, is that correct?

A That's correct.

Q Now, doesn't the earnings as a percentage of total value reflect whatever factors are present in determining a market value?

A I don't think that I quite understand the question.

Q All right. Market value takes into consideration all of the factors that may exist that determines the market price of the stock?

A Yes, and one of those is earnings, is that what you are saying?

Q One of them is earnings, but when you take now, a percentage of earnings to market value, and the market values takes into consideration all the factors, that determine the market price when you finally get that percentage, as you have here 4.68 for Martha White, or 8.77 for Manischewitz, aren't you taking into consideration all of the factors that have affected market price of which the earnings figure is expressed as a percentage of?

A I still don't understand the question.

Q All right, let's try it again. Market --

A Well, don't just repeat it in the same way, because I don't think that I will ever understand it.

Q The market price takes into consideration all the factors, sales, net worth, earnings, dividends, whatever goes into -- growth factor, sponsorship, floating supply, whatever factors go into determining market price are reflected in the total value, is that right?

A Yes, that's right.

Q All right. Now, when you express earnings as

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a percentage of that market price, you are getting a certain percentage that the earnings represent of -- of the market price or the total value where the total value already has all of the factors that affect the price in it.

A Well, maybe -- maybe -- maybe there is a misunderstanding as to what this percentage of total value really is, it is just step one in the mathematical step converting ultimately to a multiplier.

Q All right, it is column, one, two, three, four, five, six -- column six divided by column five, earnings divided by total value.

THE COURT: As the Court understands it, all it is is another way of expressing the price earnings ratio.

MR. GELFAND: The price earnings ratio.

THE COURT: That's all that it is.

BY MR. GELFAND: (Resuming)

Q And, in your net worth, you have got a price net worth ratio, and in your sales percentage you have got a price over sales ratio.

A Right.

Q All right. Now, if we were to take your composite figures, of 5.57 percent, total composite data, 40.50 percent and 170.92, and obtain the reciprocals, and divide

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by three, and multiply each one times the base figure, earnings, net worth, and sales, we do come out with the 44 million, do we not?

A Yes, 44 million in total value?

Q In total value.

A Yes.

Q All right. Then, I would like to know why since each one of these factors represents the ratios to the total value, including all the factors that determine total value, why did you go and weigh one more than the other?

A Why did I weight earnings more than net worth and sales?

Q That's right.

A Because I felt that that's the most important factor in --

Q But your earnings are already expressed as a percentage of earnings value, in other words all the factors that go into market value are in there, each one is expressed as a percentage of the market value?

A There is a definite lack of understanding on my part on what point you are making now, I really don't follow this point.

Q You weighted --

THE COURT: Why don't we let the schedule speak

for itself, Mr. Gelfand?

MR. GELFAND: All right.

THE COURT: The schedule shows what he has done.

BY MR GELFAND: (RESuming)

Q Didn't any question arise in your mind in your method of appraisal when you start with companies in quite different pursuits and your chart shows a variation of more than 2 to 1 in the price earnings ratio, of approximately 5 to 1 in the price net worth ratio, and 2 1/2 to 1 in the price sales ratio? In other words you have for Martha White on net worth a 26 percent return on market value, and in Manischewitz where the market price doesn't even equal the net worth of the company, doesn't any question arise regarding either the type of company selected or the method being used?

A Well, of course I wished that they were closer together, I wished they all were in a very tight bracket, it would be very nice. I think that we must realize that we are using more than one factor, we are using three factors, and if we consider that earnings, net worth and sales are some kind of contributory components of value, then we must realize that -- that a company that has for example lower earnings, but a very high net worth, that high net worth might offset to some degree the lower earnings -- you know, that there is an interplay here, and you can't genera-

lize it in the way that you just have.

Q But, that's what I was trying to get when I asked you the first question, but isn't that interplay with respect to earnings already reflected when you take a percentage of earnings to the market value and the market value has all the other factors already in it? Isn't it --

MR. GOLDBERG: Your Honor, the witness hasn't answered the --

MR. GELFAND: All right.

THE COURT: Well, as the Court understands it, counsel, all counsel is saying is that the -- is that the price earnings ratio reflects risk, financial condition, and like that, I think that he has got in mind its current assets, and that undoubtedly is going to be reflected in the price, Martha White presumably has got a lot more seasoning, more established company, larger volume, and you expect probably a much more secure sales volume too for that matter. That's going -- everything is going to be reflected in the price earnings ratio, I would think.

BY MR. GELFAND: (Resuming)

Q Mr. MacMullan, doesn't this chart consider what the different activities that the companies are in, isn't it really like taking pears, apples, bananas, pineapple, making a fruit salad, and comparing it to the one ingredient,

apples, because there is a single underlined thing, its fruit?

A Well, I think that I have really expressed myself as to what I feel, how valid the comparables are, you know, several times. And, it is just another way of asking me the same question.

Q Well, are you saying it doesn't or it does in answer to my question?

A Well, repeat your question --

MR. GELFAND: Please read it back.

(Whereupon, the reporter played back the portion requested.)

THE COURT: Let's answer the question in the affirmative, and get along here.

MR. GELFAND: All right.

THE COURT: I think Mr. Gelfand, that that's why the Court came back to the basic proposition that if you want to -- you want to get into the ultimate of the valuation study here, there are so many factors that are missing that the Court would be inclined to -- to entertain a motion that we strike all of them frankly. I think that the -- you don't do everything in every case. You could carry this company back a lot farther, I think, the longer the history the more -- the more reliable might be the projections. I think that you would have to tie it in with

economic indices, and somebody would have to project the future, and there so many things if you are going to use that type of approach, that you stop somewhere and accept the results subject to the qualifications, that if you wanted to use that Econometric Model up at Harvard, and spend $100,000.00, you might come up with another answer, but I'm not so sure that they would be any closer to being right than somebody else, they just over argue with what they do.

MR. MUSOFF: Your Honor, --

THE COURT: It's a sliderule game, when you get right down to it.

MR. MUSOFF: Your Honor, may I just make one or two comments?

THE COURT: Yes.

MR. MUSOFF: At the risk of ~~opposing~~ exposing my ignorance, I can't hold a candle either to the Court or Mr. Gelfand when it comes to statistics or anything of that nature, and it therefore seems to me that the thing that has most validity in these situations is the marketing concept, what something would actually sell for in the pragmatic scheme of life, and --

THE COURT: That's -- that's why I like the Ladenburg, Thalm report.

MR. MUSOFF: And --

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THE COURT: That's closer to reality in the marketplace.

MR. MUSOFF: Except, Your Honor, that the whole situation changed by 1969. It would seem to me, that if I owned a company, Your Honor, and I'm no whiz as a readily admit when it comes to finance, but if I owned a company such as Mr. Jack Silverman owned, and I had an opportunity to unload non-voting shares and retain complete control of my company, it would seem to me that I would jump at the chance of selling it at 2 to $5.00 a share, because what am I doing, I'm getting -- it is better than going public. I'm still the sole manager of the assets. I'm retaining control, I don't have to answer to anybody. I don't have to get involved with the SEC, and it seems to me that pragmatically, if someone -- if -- like some investment banker came to me and said in your recapitalization, you have got so many thousands of shares of non-voting -- stock --

THE COURT: You can put that in your brief, but let me just point out one thing, you are talking about -- you are talking about,probably about what his annual salary was. There would be no point in selling what amounted to 40 percent of the underlying interest in the company for a year's salary, would there?

MR. GELFAND: It doesn't work out that way, Your

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Honor, Mr. Silverman still had $1,370 -- let's see, $1,370,000.00 worth of preferred stock that was paying him a $5.00 dividend.

THE COURT: We can all work these figures out, but I say --

MR. GELFAND: You still --

THE COURT: Let's keep ourselves on -- on the question that we have before us now, and that is Mr. Gelfand's cross examination of which I think he is doing quite effectively, and it goes to the question as to how much weight -- what was the depth of the investigation let us say upon which this appraisal was based.

The witness frankly testified that he took Moody's and he flipped through Moody's and he picked what he thought was probably about as close a fruit to the apple as he could get, and he threw them all in the pot, and then he exercised his judgment, and he comes out with a figure. And, I think that one of the Petitioner's witnesses with a few variations followed the same approach, because when the -- when the American Appraisal figure witness got down to discounting, he didn't say why he discounted this one more or less than others, he had a range there, and he reaches out of the wild blue, and he pulls out a figure, and he says, I discount it this much.

But, I mean, all of that goes to the exercise of

> event took place, all that the donees received was a nonvoting interest in a family controlled corporation.

But then the Court proceeded to do what it stated it was not to do. In valuing the shares, it referred to the future public offering which even the Court itself recognized was brought about by a transaction occurring after the time of the gifts and not foreseen at the time of the gifts.(3)

The Court's advent into the realm of speculation about the donee's contemplation in September and October 1968 to "go public" at some future unspecified date, concerning which there isn't a scintilla of supportive evidence, was specifically banned by the Supreme Court in Olson v. U.S. 292 U.S. 246 (1934) when it stated (p.257)

> "Elements affecting value that depend upon events or combinations of occurrences which, while within the realms of possibility, are not clearly shown to be reasonably probable should be excluded from consideration, for that would be to allow mere speculation and conjecture to become a guide for the ascertainment of value -- a thing to be condemned in business transactions as well as in judicial ascertainment of truth." (emphasis added)

The Tax Court further stated:

> "The expert testimony presented by the petitioners failed to take into account the fact that if petitioners intended to sell

(3) p. 21

> a substantial interest in Modern Maid -- and the Class B stock represented approximately two-thirds of the equity after the preferred stock -- they would have adopted a different course of action or there never would have been a sale."(4)

Such "different course of action" for valuing the stock would convert the property into something other than what the petitioners were giving. To adopt a "different course of action", not set out by the Court, but presumably a public offering, would

(a) No longer be the property which was the actual subject of the gift, but some entirely different property, and

(b) Not be possible with non-voting stock.

To use publicly owned voting stock as the basis for valuation would be not only a horse of a different color, but an entirely different animal. It would represent loss of control by the donors of their company. This is something they were unwilling to do in any event -- even with respect to gifts to their own children.

2. The Tax Court erred in its rejection of the truly expert testimony of Herbert Cannon and Harold Wit with notable credits and long active experience in the advising

(4) p. 24

about and marketing of securities in the financial community. The testimony of such experts was not diminished upon cross examination or negated by contradictory evidence with respect to their special expertise. This testimony was rejected not because it wasn't valid, but only because the Court was of the opinion the donees would have marketed their stock in a different fashion or there wouldn't be any sale at all.

This argument of the unwillingness of a donor to sell at the price a willing buyer would pay was raised by the government in Whitmore v. Fitzpatrick 127 F. Supp. 710 (Conn. 1954), but rejected by that Court. In that case the Court found the fair market value of the underlying assets was $3,118 per share. Taxpayer's experts' testimony of obtainable market price ranged from $850 to $1200 per share for minority interests (a total of 73% had been given to three sons). The government argued the plaintiff, as the sole owner, would not be a willing seller at the only price which a buyer according to plaintiff's experts would buy. The Court (Judge Hincks) stated: "Surely this argument is irrelevant to the problem".

The District Court stressed the "extraordinary difficulty in finding a buyer who would invest something over $200,000 (200 shares at $1000 a share) in a minority

interest" in a company without an established dividend paying record. The District Court presumptively rejected the theory that a larger sum could be realized if a different method of marketing had been pursued by first converting the property into something else.

Imagine what difficulty would then exist to find two buyers who would pay more than $640,000 each (25,680 shares x $25) to buy minority interests of non-voting stock without a market in a company making prepared batter mixes and crumbs for breading! Jack Silverman's gifts were to 2 donees and Seymour Silverman's gifts were to 3 donees, not hundreds or thousands of donees, and the gifts should be valued accordingly. (5)(30

The Court failed to recognize that the different course of action to which it was referring would have involved a great many purchasers and would have been illegal at that time without a registration with the Securities and Exchange Commission. Such a registration and such marketing would have converted the property that was actually given to

(5) The Court itself expressed the opinion that Modern Maid Food Products, Inc. stock "wasn't the type of business that would attract so-called venture capital anyway;" (Tr. 235) and that parties with venture capital are not attracted to the type of business of Modern Maid Food Products, Inc. (Tr. 236). In both of these opinions the Court's opinion was confirmed by Herbert Cannon, an expert in raising venture capital. (Tr. 235, 236)

property of a different kind.[6] It is important to note that Section 25.2512-1 of the Commissioner's own regulations defines fair market value as "that price at which property would change hands between a willing buyer and a willing seller" - just one buyer not many buyers for each gift of stock in a closely held corporation. Rejecting the testimony of Herbert Cannon and Harold Wit, which was based on the nature of the property actually given, for the reason stated by the Court is, therefore, making a finding clearly contrary to the weight of the evidence.

3. Appraisal reports and testimony had been submitted by both respondent's and one of petitioners' experts using the price-earnings method of evaluation based on alleged comparable companies. Both experts applied this price-earnings ratio to total corportate net income from which was subtracted

(a) The estimated cost of the public offering.

(b) The value of the preferred stock.

(c) Discount(s) for minority interest and Class B stock infirmities.

The petitioners definitively demonstrated the inapplicability of the appraisal of respondent's expert[7] and the Court

(6) Just as gifts of closely held stock may not be aggregated for valuation (Whitemore v. Fitzpatrick, supra, William Rushton, et al. 60 TC 272, reviewed by the Court and affirmed 5th Cir. 7/26/74), they may not be broken up for valuation, particularly when such breakup would be a violation of the Securities and Exchange Act or a conversion into different property.

(7) Petitioners' Brief pp. 26-41

was of similar opinion at the time of trial.[8]

The Court in its findings of fact stated:

> "A multiple of ten times average earnings was a reasonable basis for valuation of the Class A Common stock of Modern Maid."

No basis for this finding was given or exists in the record. Petitioners' expert, Gordon Smith of the American Appraisal Company did use that multiple of earnings in his report, but that was a multiple of total corporate earnings based upon an assumed public offering and from which initial total value deductions were taken for the cost of going public, the value of the preferred stock and the discount applicable to minority interest and Class B stock infirmities. The Court has used the same ten times earnings multiple, but applied it to the pro-forma earnings per share of Modern Maid Food Products, Inc., as if Modern Maid Food Products, Inc. was already a public company, which it wasn't, and without making the deductions used by both Respondent's and Petitioners' experts. If these deductions were made, a quite different valuation would result.

The government's expert used an 8% factor for cost of going public. He admitted that was purely for underwriting.

(8) Tr. p.190 - The Court "I think Mr. Gelfand that that's why the Court came back to the basic proposition that if you want to, ... there are so many factors missing that the Court would be inclined to entertain a motion that we strike all of them (the appraisals) frankly."

writing cost. He didn't know any company other than Modern Maid Food Products, Inc. that paid only 8% for an underwriting in 1968 or 1969 for a small offering. In addition, there are costs for legal fees, accounting fees and administrative costs. Mr. Smith, petitioners' expert, taking these other costs into consideration used a cost factor of 15% which percent was supported by the testimony of Herbert Cannon with vast experience in the underwriting field. It is pertinent to note that in Inga Bardahl TCM 1965-158, the respondent's own expert discounted the price-earnings determination of fair market value by 20% for the cost of going public.

The government's only expert witness in this case stated discounts for minority interests vary from 10% to 50% from otherwise fair market value. He used a 25% discount factor computed on his schedule on page 50 of his appraisal report. The non-applicability of his comparatives as well as the mathematicl errors have been commented upon at length in petitioners' original brief.

The cases cited by government's own expert in Exhibit Q relfect the following percentages of discount for minority interest.

Drybrough v. U.S.	35%
Obermer v. U.S.	33 1/3%

The actual purchases of twelve minority interests by the Value Line Development Corp. in January - July 1968 are set out in Exhibit 18 in a schedule entitled "Exhibit 3." This data was for restricted shares of publicly traded securities and thus enjoyed a somewhat more favorable position than a minority interest in a closely held corporation with no market for its shares.

The Discounts for minority interests in this chart vary from a low of 16.7% to a high of 71.4% with a mean of 44% and a median of 42%.

Toward the end of 1969 when Modern Maid Food Products, Inc. became publicly owned, a discount of 8% was recognized for the Class B Common stock from the Class A Common stock, although Mr. MacMullen determined a discount of 16 2/3% or a maximum of $5 a share.

Applying these facts to a ten times earnings valuation if public, gives the following result:

Average earnings of 4 years prior to the gifts	$	570,000
Value of Company (10 times earnings)		5,700,000
Less Cost of going public -15%		850,000
Balance	$	4,850,000
Preferred stock		2,520,000
Value to common stock	$	2,330,000
Value per share (÷ 112790)	$	20
Discount for minority interest 35%		7
	$	13
Discount for Class B Limitation-8%		1
Value Class B Common stock -	$	12

Using the government expert's return on net worth approach, which method eliminates the vagaries of the market place, and correcting for mathematicl and other errors in Mr. MacMullen's use of the data, gives the following result:

Comparables' average of net income as a percent of net worth at the beginning of the year was 17.62% (see petitioners' brief pp. 28, 29)

	1/1/68	6/30/68
Net Worth per books	3,850,000	4,200,000
Comparables' % of return	17.62%	17.62%
Relative Net Income	$ 678,000	$ 740,000
Earnings - 6 mos. $380,000 x 2	760,000	760,000
Excess Earnings	82,000	20,000
Capitalized at avg.rate of return	17.62%	17.62%
Goodwill	465,000	110,000
Net Worth per Books	3,850,000	4,200,000
Value of Company	4,315,000	4,310,000
Preferred stock	2,52 ,000	2,520,000
Balance of Common Stock	1,795,000	1,790,000
Computed value of common stock	$ 1,800,000	
÷ 112,790 shares	$16 a share	
Discount for minority interest and no market-35%	5.60 "	
	10.40	
Discount for Class B limitations-8%	.80	
Value Class B Common stock	$ 9.60	

4. The Court also erred in its application of the burden of proof rule. Once the Commissioner acknowledged that his original $48 a share value determination was in error, his presumption of correctness disappeared as the Court noted.(9)

When the determination of the Commissioner is found to be invalid, the determination made by the Tax Court "must be based upon substantial evidence and it is incumbent upon the Commissioner, not the taxpayer, to come forward with that evidence."(10) (emphasis added)

To the same effect is the decision in Helvering v. Taylor 70 F. 2d 619 (2nd Cir. 1934) affirmed 293 U.S. 507 (1935). In the Taylor case the Court of Appeals for the Second Circuit said:

> "If the burden of proof goes so far as to demand not only that the taxpayer show that the deficiency assessed against him is wrong, but what is the proper deficiency, or that there should be none at all, the decision (B.T.A.) was right even though we know the tax is too high. In an action to recover taxes unlawfully collected the burden does go so far. (citations) But the reason for this is obvious; a plaintiff, seeking an affirmative judgment measured in dollars, must prove how much is due. His claim is for money paid and he must show that every dollar he recovers is unjustly withheld. So it is not enough merely to prove

(9) Tr. 207.

(10) Kaufman v. Commissioner 18 AFTR 2d 6031 (4th Cir. 1966). This rule may not apply in the case of deductions.

that the tax as a whole was unlawful; some of the dollars he paid may nevertheless have been due. But this reasoning does not apply when the proceeding is to review an assessment. Although that does indeed partake of the nature of a judgment, and the taxpayer has the burden of proving that it was wrong, after he has done so, he need not, at least under ordinary principles of procedure, prove that he owed no tax, or what was the tax that he did owe. The original assessment rested upon a finding, presumptively correct, but the presumption of its correctness does not extend to other findings which the Commissioner has never made. Any other result would invert the ordinary rules of procedure by imposing a burden of establishing a negative upon the obligor; indeed of disproving the existence of all possible obligations. (emphasis supplied)

In Federal National Bank of Shawnee, Oklahoma v. Commissioner 180 F. 2d 494 (10th Cir. 1950) the Court stated:

> "The burden of proof was on the taxpayer to show that the Commissioner's determination was invalid, but to meet that burden it was sufficient for the taxpayer to show that the determination was excessive and invalid. The taxpayer was not required to prove that he owed no tax or the correct amount of tax he did owe. It may not be held that he is bound to pay a tax that confessedly he does not owe, unless his evidence was sufficient also to establish the correct amount of tax, if any, that might be lawfully exacted." (emphasis added)

See also A & A Tool & Supply Co. et al. v. Commissioner 182 F. 2d 300 (10th Cir. 1950)

In the instant case the Commissioner's determination in the statutory notice was admittedly in error when he opted for $25 a share instead of the original $48 a share.

Despite the burden of proof now being on the Commissioner, the Tax Court holds petitioners' proof that "going public" was not foreseen at the time of gift "does not negate the respondent's claim that petitioner's future plans went beyond the first step, with which we are here concerned."(11)

The Court also stated "Although Ladenberg, Thalmann & Co. was unquestionably the best qualified 'expert' to express an opinion with respect to value of the stock of Modern Maid, petitioners chose not to present the testimony of the firm."(12)

Petitioners submit the burden of proof being upon the Commissioner, once he acknowledged error in his original determination, it was not incumbent upon them to disprove a mere "claim" of the respondent with respect to petitioners' future plans, or to call Ladenberg, Thalmann & Co.

(11) T.C. Opinion, p. 21, fn. 4

(12) ~~p. 24~~

even assuming they were the best qualified experts to value the kind of stock given as a gift in 1968.

With respect to future plans of "going public", the record does contain the following.

Q. "Up to and including the time of the gifts, did you have any intention for Modern Maid Food Products, Inc. to become a publicly owned corporation or to merge or sell said corporation? (emphasis added)

A. (Jack Silverman) No, there was not."

There is no basis in the record nor has respondent or the Court even intimated any challenge to the credibility of Jack Silverman. In fact the only evidence in the record on this point (exhibits and testimony) shows that going public was a happenstance arising out of events occurring after the gifts were made.(14) The respondent submitted no proof that the petitioners at the time of the gifts contemplated going public at some future unspecified date.

The Courts alluding to petitioner's responsibility and failure to call Ladenberg Thalmann & Co. is unwarranted since respondent had the burden of proof.(15)

(13) Tr. 13

(14) p. 21 fn 4

(15) Respondent's efforts to contact a knowledgeable party from Ladenberg, Thalmann & Co. were fruitless since such party was no longer available, being somewhere in Texas.

5. In its reply brief petitioners posed a question containing the statement "knowing that the substantial salaries and preferred dividends vitiated any incentive to declare dividends on the common stock".

The Court has interpreted those words to imply "an intent to refrain from declaring dividends, increasing their salaries at will and otherwise acting to the detriment of non-voting shareholders" and proceeds to demolish that straw man. The fact is that the receipt of substantial salaries and preferred dividends does weaken the incentive to declare common stock dividends; such failure to declare dividends need not be violative of a quasi-fiduciary relationship. Any knowledgeable buyer of such shares would be aware of such condition which would obviously affect the price he would be willing to pay. Who wants to buy into a company for the purpose of charging and proving violations of a quasi-fiduciary relationship? As a matter of fact the record shows no dividends have been declared on the common stock of Modern Maid Food Products, Inc. after December 31, 1967 to the time of trial in 1974.

6. Petitioners recognize that values in any particular case are factual and specific to a particular case, but the opinion and determination of the Court has

no precedent in any guidelines heretofore set out by other courts, upon which guidelines, taxpayers and their counsel have a right to rely.

In Righter v. United States (Ct.Cl. 1961) 439 F. 2d 1204, there is the following comment:

> "The Comparative Appraisal method produces, nevertheless, no magic formula which rigidly gives the exact valuation answer. Companies are rarely identical in size, operation, or product and allowances must be made as the statute says, for 'all other factors'. This would necessarily include the very fact of unmarketability of the stock of a closely held corporation. In the last analysis much necessarily depends on the informed judgment of the knowledgeable investor concerning the refinements and adjustments to be made in arriving at the ultimate valuation figure. Thus it is not surprising that in this field the opinions of experts are considered to be peculiarly appropriate. (emphasis supplied)

In Whitemore v. Fitzpatrick (Conn. 1954) 121 F. Supp. 710, Judge Hincks agreed that power of control, liquidity of the investment, opportunities to revamp business and asset holdings, net return by way of dividends as compared with other opportunites in the open market, the tax aspects of the purchase are the factors a level-headed investor contemplating a large investment would make. The Court stated:

> "In view of the lack of market for the stock, there would be extraordinary difficulty in finding a buyer who would invest something over $200,000 in a minority interest in a Naugatuck corporation such as the Whitemore Company without an established

> dividend record of which about one-quarter in value of assets was in non-liquid form."

It should be noted the Court found the actual value to be $3118 per share, but the fair market value to be only $1057 per share, a discount of 66% for three closely held minority interests which formed a 73% majority in the aggregate.

In Estate of Gregg Maxcy T.C. Memo 1969-158 the Court stated:

> "In the instant case we are attempting to determine a price a willing seller of Maxcy Securities shares could get from a willing buyer, not what a buyer may eventually realize." (emphasis supplied)

In Richard Makeoff T.C. Memo 1967-13, 99% of the total common stock capitalization represented by non-voting stock was ascribed a value of 60% of the total capitalization -- in effect a discount of almost 40% solely due to its being non-voting stock.

In Morris Messing 48 T.C. 502, (1967) stock was sold to an underwriter on June 15, 1961 at a price equal to $9.80 a new share. The stock was split on June 30, 1961 preparatory to going public, gifts were made on September 13th and 16th, 1961 and a registration statement filed with the S.E.C. on September 27th, 1961. The respondent in

valuing the stock used as a starting point the market value when the company became publicly owned, less than 4 months after the date of the gifts.

The Court in that case rejected this approach stating "a publicly traded stock and a privately traded stock are not as respondent would have us assume, the same animal distinguished only by size, frequency or color of its spots. The essential nature of the beast is different." The Court further stated:

> "It is a matter of common knowledge that, as a result of the vagaries of the stock market and other national and international events, many a contemplated public offering never sees the light of day, and that because of factors effecting the market at the particular moment of the public offering, the offering price can be radically different from the one originally contemplated. In September 1961, there was no probable basis for predicting a public offering would in fact take place and even less for estimating the particular price of the offering."

If this is true in a case where a preliminary registration is made during the month of the gift, how remote and speculative are the possibilities where a public issue is never even contemplated at the time of the gifts, events happen that lead to negotiations beginning 7 months later, and the public offering is 14 months later?

See also Bruce Berckmanns T.C. Memo 1961-100 and the principles enunciated therein.

Petitioners feel particularly aggrieved with the opinion of the Court since at the Court's urging effective settlement negotiations had been undertaken by the parties' counsel with respect to both 1968 and 1969 claimed gift tax deficiencies. Counsel had tentatively agreed on a basis of settlement of stock value of $10 a share for 1968, which would result in no deficiencies for that year, and an additional constructive gift of $4 a share in 1969 as a result of the reorganization. Settlement for 1969 was subject to agreement by the appellate division of the Internal Revenue Service since the trial of the deficiencies for 1969 had not yet been calendared. The settlement values were in accord with principles contained in advice from the national office of the Internal Revenue Service.

Report to the Court of settlement progress was awaiting a call from the Court, when the Court's opinion was received setting a value of $25 a share.

WHEREFORE it is prayed that this motion be granted.

Respectfully submitted,

Sidney Gelfand

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Dated: November 25, 1974.

UNITED STATES TAX COURT

SEYMOUR SILVERMAN, Petitioner,	)	
v.	)	Docket No. 3707-72
COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $43,890.00.

(signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

By: _____
GERALD BACKER,
Act'g Asst. Regional Counsel,
26 Federal Plaza (12th Fl.),
New York, New York 10007,
Tel. No. 212-264-8134.

/s/ Sidney Gelfand
SIDNEY GELFAND,
Counsel for Petitioner,
136 East 57th Street,
New York, New York 10022,
Tel. No. 212-753-2900.

UNITED STATES TAX COURT

HELEN SILVERMAN, Petitioner,	)	
v.	)	Docket No. 3708-72
COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $43,890.00.

(Signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

By: /S/
GERALD BACKER,
Act'g Asst. Regional Counsel,
26 Federal Plaza (12th Fl.),
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Sidney Gelfand
SIDNEY GELFAND,
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136 East 57th Street,
New York, New York 10022,
Tel. No. 212-753-2900.

UNITED STATES TAX COURT

JACK SILVERMAN,	)	
	)	
Petitioner,	)	
	)	
v.	)	Docket No. 3709-72
	)	
COMMISSIONER OF INTERNAL REVENUE,	)	
	)	
Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $94,395.00.

(Signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

/s/ Sidney Gelfand
SIDNEY GELFAND,
Counsel for Petitioner,
136 East 57th Street,
New York, New York 10022,
Tel. No. 212-753-2900.

By: _____
GERALD BACKER,
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26 Federal Plaza (12th Fl.),
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Tel. No. 212-264-8134.

UNITED STATES TAX COURT

FRANCES SILVERMAN, Petitioner,	)	
v.	)	Docket No. 3710-72
COMMISSIONER OF INTERNAL REVENUE, Respondent.	)	

DECISION

Pursuant to the opinion of the Court filed November 6, 1974, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED and DECIDED: That there is a deficiency in gift tax due from the petitioner for the taxable year 1968 in the amount of $94,395.00.

(signed) William H. Quealy

Judge.

Entered: MAY 20 1975

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the respondent's computation, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein.

/s/ Sidney Gelfand

SIDNEY GELFAND,
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136 East 57th Street,
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Tel. No. 212-753-2900.

MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.

By: _____

GERALD BACKER,
Act'g Asst. Regional Counsel,
26 Federal Plaza (12th Fl.),
New York, New York 10007,
Tel. No. 212-264-8134.

STATUTE, LAW AND REGULATIONS

CONSTITUTION OF THE UNITED STATES

V AMENDMENT

"No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any Criminal Case to be a witness against himself, nor be deprived of life, liberty or property, without due process of law; nor shall private property be taken for public use, without just compensation." (Emphasis Supplied)

STATUTES

UNITED STATES Code, TITLE 15
Sec. 77d. Exempted transactions

The provisions of section 77e of this title shall not apply to--

(1) transactions by any person other than an issuer, underwriter, or dealer.

(2) transactions by an issuer not involving any public offering.

(3) transactions by a dealer (including an underwriter no longer acting as an underwriter in respect of the security involved in such transaction), except--

(A) transactions taking place prior to the expiration of forty days after the

first date upon which the security was bona fide offered to the public by the issuer or by or through an underwriter,

* * * *

Sec. 77e. Prohibitions relating to interestate commerce and the mails

*a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly--

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly--

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security with respect to which a registration statement has been filed under this sub-chapter, unless such prospectus meets the requirements of section 77j of this title; or

(2) to carry or cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of subsection (a) of section 77j of this title.

(c) It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the

use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 77h of this title.

UNITED STATES CODE, TITLE 26.

Sec. 2512 - VALUATION OF GIFTS

(a) If the gift is made in property, the fair market value thereof at the date of gift shall be considered the amount of the gift.

REGULATIONS UNDER INTERNAL REVENUE CODE

Sec. 25.2512-1. Valuation of property; in general

Section 2512 provides that if a gift is made in property, its value at the date of the gift shall be considered the amount of the gift. The value of the property is the price at which such property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell, and both having reasonable knowledge of relevant facts. The value of a particular kind of property is not the price that a forced sale of the property would produce. . .

Sec. 25.2512-2. Stocks and bonds--(a) In general. The value of stocks and bonds is the fair market value per share or bond on the date of the gift.

(b) Based on selling prices. (1) In general, if there is a market for stocks or bonds, on a stock exchange, in an over-the-counter market or otherwise, the mean between the highest and lowest quoted selling prices on the date of the gift is the fair market value per share or bond. If there were no sales on the date of the gift but there

were sales on dates within a reasonable period both before and after the date of the gift, the fair market value is determined by taking a weighted average of the means between the highest and lowest sales on the nearest date before and the nearest date after the date of the gift. The average is to be weighted inversely by the respective numbers of trading days between the selling dates and the date of the gift....

MISCELLANEOUS

Please note that Section 4(1) of the Securities Act of 1933 has been renumbered as Section 4(2)

For RELEASE Tuesday, November 6, 1962

SECURITIES AND EXCHANGE COMMISSION
Washington 25, D. C.

SECURITIES ACT OF 1933
Release No. 4552

NON-PUBLIC OFFERING EXEMPTION

The Commission today announced the issuance of a statement regarding the availability of the exemption from the registration requirements of Section 5 of the Securities Act of 1933 afforded by the second clause of Section 4(1) of the Act for "transactions by an issuer not involving any public offering," the so-called "private offering exemption." Traditionally, the second clause of Section 4(1) has been regarded as providing an exemption from registration for bank loans, private placements of securities with institutions, and the promotion of a business venture by a few closely related persons. However, an increasing tendency to rely upon the exemption for offerings of speculative issues to unrelated and uninformed persons prompts this statement to point out the limitations on its availability.

Whether a transaction is one not involving any public offering is essentially a question of fact and necessitates a consideration of all surrounding circumstances, including such factors as the relationship between the offerees and the issuer, the nature, scope, size, type and manner of the offering.

The Supreme Court in S.E.C. v. Ralston Purina Co., 346 U.S. 119, 124, 125 (1953), noted that the exemption must be interpreted in the light of the statutory purpose to "protect investors by promoting full disclosure of information thought necessary to inform investment decisions" and held that "the applicability of Section 4(1) should turn on whether the particular class of persons affected need the protection of the Act." The Court stated that the number of offerees is not conclusive as to the availability of the exemption, since the statute seems to apply to an offering "whether to few or many." 1/ However, the Court indicated that "nothing prevents the Commission, in enforcing the statute, from using some kind of numerical test in deciding when to investigate particular exemption claims." It should be emphasized, therefore, that the number of persons to whom the offering is extended in relevant only to the question whether they have the requisite association with and knowledge of the issuer which make the exemption available.

Consideration must be given not only to the identity of the actual

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1/ See, also, Gilligan, Will & Co. v. S.E.C., 267 F. 2d 461, 467 (C.A. 2, 1959), cert. denied, 361 U.S. 896 (1960).

purchasers but also to the offerees. Negotiations or conversations with or general solicitations of an unrestricted and unrelated group of prospective purchasers for the purpose of ascertaining who would be willing to accept an offer of securities is inconsistent with a claim that the transaction does not involve a public offering even though ultimately there may only be a few knowledgeable purchasers. 2/

A question frequently arises in the context of an offering to an issuer's employees. Limitation of an offering to certain employees designated as key employees may not be a sufficient showing to qualify for the exemption. As the Supreme Court stated in the Ralston Purina case: "The exemption as we construe it, does not deprive corporate employees, as a class, of the safeguards of the Act. We agree that some employee offerings may come within Section 4(1), e.g., one made to executive personnel who because of their position have access to the same kind of information that the Act would make available in the form of a registration statement. Absent such a showing of special circumstances, employees are just as much members of the investing 'public' as any of their neighbors in the community." The Court's concept is that the exemption is necessarily narrow. The exemption does not become available simply because offerees are voluntarily furnished information about the issuer. Such a construction would give each issuer the choice of registering or making its own voluntary disclosures without regard to the standards and sanctions of the Act.

The sale of stock to promoters who take the initiative in founding or organizing the business would come within the exemption. On the other hand, the transaction tends to become public when the promoters begin to bring in a diverse group of uninformed friends, neighbors and associates.

The size of the offering may also raise questions as to the probability that the offering will be completed within the strict confines of the exemption. An offering of millions of dollars to non-institutional and non-affiliated investors or one divided, or convertible, into many units would suggest that a public offering may be involved.

When the services of an investment banker, or other facility through

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2/ Reference is made to the so-called "investment clubs" which have been organized under claim of an exemption from the registration provisions of the Securities Act of 1933 as well as the Investment Company Act of 1940. It should not be assumed that so long as the investment club, which is an investment company within the meaning of the latter Act, does not obtain more than 100 members, a public offering of its securities, namely the memberships, will not be involved. An investment company may be exempt from the provisions of the Investment Company Act if its securities are owned by not more than 100 persons and it is not making and does not presently propose to make a public offering of its securities. (Section 3(c)(1)). Both elements must be considered in determining whether the exemption is available.

which public distributions are normally effected, are used to place the securities, special care must be taken to avoid a public offering. If the investment banker places the securities with discretionary accounts and other customers without regard to the ability of such customers to meet the tests implicit in the Ralston Purina case, the exemption may be lost. Public advertising of the offerings would, of course, be incompatible with a claim of a private offering. Similarly, the use of the facilities of a securities exchange to place the securities necessarily involves an offering to the public.

An important factor to be considered is whether the securities offered have come to rest in the hands of the initial informed group or whether the purchasers are merely conduits for a wider distribution. Persons who act in this capacity, whether or not engaged in the securities business, are deemed to be "underwriters" within the meaning of Section 2(11) of the Act. If the purchasers do in fact acquire the securities with a view to public distribution, the seller assumes the risk of possible violation of the registration requirements of the Act and consequent civil liabilities. 3/ This has led to the practice whereby the issuer secures from the initial purchasers representations that they have acquired the securities for investment. Sometimes a legend to this effect is placed on the stock certificates and stop-transfer instructions issued to the transfer agent. However, a statement by the initial purchaser, at the time of his acquisition, that the securities are taken for investment and not for distribution is necessarily self-serving and not conclusive as to his actual intent. Mere acceptance at face value of such assurances will not provide a basis for reliance on the exemption when inquiry would suggest to a reasonable person that these assurances are formal rather than real. The additional precautions of placing a legend on the security and issuing stop-transfer orders have proved in many cases to be an effective means of preventing illegal distributions. Nevertheless, these are only precautions and are not to be regarded as a basis for exemption from registration. The nature of the purchaser's past investment and trading practices or the character and scope of his business may be inconsistent with the purchase of large blocks of securities for investment. In particular, purchases by persons engaged in the business of buying and selling securities require careful scrutiny for the purpose of determining whether such person may be acting as an underwriter for the issuer.

The view is occasionally expressed that, solely by reason of continued holding of a security for the six-month capital-gain period specified in the income-tax laws, or for a year from the date of purchase, the security may be sold without registration. There is no statutory basis for such assumption. Of course, the longer the period of retention, the more persuasive would be the argument that the resale is not at variance with an original investment intent, but the length of time between acquisition and

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3/ See Release No. 33-4445.

resale is merely one evidentiary fact to be considered. The weight to be accorded this evidentiary fact must, of necessity, vary with the circumstances of each case. Further, a limitation upon resale for a stated period of time or under certain circumstances would tend to raise a question as to original intent even though such limitation might otherwise recommend itself as a policing device. There is no legal justification for the assumption that holding a security in an "investment account" rather than a "trading account," holding for a deferred sale, for a market rise, for sale if the market does not rise, or for a statutory escrow period, without more, establishes a valid basis for an exemption from registration under the Securities Act. 4/

An unforeseen change of circumstances since the date of purchase may be a basis for an opinion that the proposed resale is not inconsistent with an investment representation. However, such claim must be considered in the light of all of the relevant facts. Thus, an advance or decline in market price or a change in the issuer's operating results are normal investment risks and do not usually provide an acceptable basis for such claim of changed circumstances. Possible inability of the purchaser to pay off loans incurred in connection with the purchase of the stock would ordinarily not be deemed an unforeseeable change of circumstances. Further, in the case of securities pledged for a loan, the pledgee should not assume that he is free to distribute without registration. The Congressional mandate of disclosure to investors is not to be avoided to permit a public distribution of unregistered securities because the pledgee took the securities from a purchaser, subsequently delinquent. 5/

The view is sometimes expressed that investment companies and other institutional investors are not subject to any restrictions regarding disposition of securities stated to be taken for investment and that any securities so acquired may be sold by them whenever the investment decision to sell is made, no matter how brief the holding period. Institutional investors are, however, subject to the same restrictions on sale of securities acquired from an issuer or a person in a control relationship with an issuer insofar as compliance with the registration requirements of the Securities Act is concerned.

Integration of Offerings

A determination whether an offering is public or private would also include a consideration of the question whether it should be regarded as a part of a larger offering made or to be made. The following factors are relevant to such question of integration: whether (1) the different offerings are part of a single plan of financing, (2) the offerings involve

4/ See Release No. 33-3825 re The Crowell-Collier Publishing Company.

5/ S.E.C. v. Guild Films Company, Inc. et al., 279 F. 2d 485 (C.A. 2, 1960), cert. denied sub nom., Santa Monica Bank v. S.E.C., 364 U.S. 819 (1960).

issuance of the same class of security, (3) the offerings are made at or about the same time, (4) the same type of consideration is to be received, (5) the offerings are made for the same general purpose.

What may appear to be a separate offering to a properly limited group will not be so considered if it is one of a related series of offerings. A person may not separate parts of a series of related transactions, the sum total of which is really one offering, and claim that a particular part is a non-public transaction. Thus, in the case of offerings of fractional undivided interests in separate oil or gas properties where the promoters must constantly find new participants for each new venture, it would appear to be appropriate to consider the entire series of offerings to determine the scope of this solicitation.

As has been emphasized in other releases discussing exemptions from the registration and prospectus requirements of the Securities Act, the terms of an exemption are to be strictly construed against the claimant who also has the burden of proving its availability. 6/ Moreover, persons receiving advice from the staff of the Commission that no action will be recommended if they proceed without registration in reliance upon the exemption should do so only with full realization that the tests so applied may not be proof against claims by purchasers of the security that registration should have been effected. Finally, Sections 12(2) and 17 of the Act, which provide civil liabilities and criminal sanctions for fraud in the sale of a security, are applicable to the transactions notwithstanding the availability of an exemption from registration.

6/ S.E.C. v. Sunbeam Gold Mining Co., 95 F. 2d 699, 701 (C.A. 9, 1938); Gilligan, Will & Co. v. S.E.C., 267 F. 2d 461, 466 (C.A. 2, 1959); S.E.C. v. Ralston Purina Co., 346 U.S. 119, 126 (1953); S.E.C. v. Culpepper et al, 270 F. 2d 241, 246 (C.A. 2, 1959).

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

SECURITIES ACT OF 1933
Rel. No. 5487 /April 23, 1974

NOTICE OF ADOPTION OF RULE 146 UNDER THE SECURITIES ACT OF 1933--
"TRANSACTIONS BY AN ISSUER DEEMED NOT TO INVOLVE ANY PUBLIC OFFERING"

(EFFECTIVE DATE: JUNE 10, 1974)

The Securities and Exchange Commission today announced the adoption of Rule 146 under the Securities Act of 1933 ("Act") which had been first noticed for comment in Securities Act Release No. 5336 (November 28, 1972) and which had been reproposed for comment in revised form in Securities Act Release No. 5430 (October 10, 1973). The adopted rule reflects a number of changes from the rule as last proposed. The changes are discussed in this release.

The Rule is designed to provide more objective standards for determining when offers or sales of securities by an issuer would be deemed to be transactions not involving any public offering within the meaning of Section 4(2) of the Act and thus would be exempt from the registration provisions of the Act. The Rule is available only to issuers since Section 4(2) provides an exemption for only the issuer. The Rule is not, however, the exclusive basis for determining whether that exemption is available. Accordingly, although persons claiming the exemption have the burden of proving its availability, persons may continue to rely on the Section 4(2) exemption by complying with the relevant administrative and judicial interpretations in effect at the time of the transaction. The protection afforded by the Rule, however, is available only to those who satisfy all its conditions.

* * * *

RULE 146

This release contains a general discussion of the background, purpose and general effect of the Rule to assist in a better understanding of its provisions. A brief analysis of each paragraph of the Rule is also included. However, attention is directed to the Rule itself for a more complete understanding.

BACKGROUND AND PURPOSE

Congress, in enacting the federal securities laws, created a continuous disclosure system designed to protect investors and to assure the

maintenance of fair and honest securities markets. The Commission, in administering and implementing these laws, has sought to coordinate and integrate this disclosure system with the exemptive provisions provided by such laws. Rule 146 is a further effort in this direction.

The legislative history of the Securities Act of 1933 indicates that the main concern of Congress was to provide full and fair disclosure in connection with the offer and sale of securities. However, Congress recognized that there were certain situations in which the protections afforded by the Act were not necessary. Concerning those specified exemptions from the Act, of which Section 4(2) is one, the House Report stated that "The Act carefully exempts from its application certain types of . . . securities transactions where there is no practical need for its application or where the public benefits are too remote."[1/]

Section 4(2) of the Act provides that "the provisions of Section 5 shall not apply to . . . transactions by an issuer not involving any public offering." The phrase "transactions . . . not involving any public offering" is not defined in the Act[2/] or, except in limited circumstances, in the existing rules under the Act. Accordingly, it has been left to Commission interpretations and court decisions to define the scope of the exemption.

The Supreme Court in the Ralston Purina[3/] case established the basic criteria to be considered in determining the availability of Section 4(2). The main consideration is whether the offerees need the protection afforded by the Act as evidenced by whether the offerees have "access" to the same kind of information that registration would disclose and whether they are able to fend for themselves. The application of these criteria and other guidelines set forth from time to time by the Commission and the courts has resulted in uncertainty about the availability of the exemption. In addition, some misconceptions have arisen in connection with certain methods used by persons who seek to claim the exemption.

For example, the questions arising under Section 4(2) have generally dealt with what constitutes a non-public offering or a private offering. It has been asserted that an offering to a limited number of persons, not more than twenty-five, for example, does not involve a public offering. This is not by itself an appropriate test. As the Supreme Court stated in Ralston Purina, "the statute would seem to apply to a 'public offering' whether to few or many." 346 U.S. at 125. The Commission continues to be of the opinion that the question is not to be determined exclusively by the number of offerees.

Further, it is frequently asserted that wealthy persons and certain other persons such as lawyers, accountants and businessmen are "sophisticated" investors who do not need the protections afforded by the Act. It is the Commission's view that "sophistication" is not a substitute for access to the same type of information that registration would provide, and that a person's financial resources or sophistication are not, without more, sufficient to establish the availability of the exemption.[4/]

On the other hand, the Commission is of the view that an offeree need not be an insider such as an officer or director of the issuer in order to have access to information. As a note to the Rule indicates, access can only exist by reason of the offeree's position with respect to the issuer. Position means an employment or family relationship or economic bargaining power that enables an offeree to obtain information from the issuer in order to evaluate the merits and risks of the investment as distinguished from situations where such position does not exist and the issuer voluntarily offers to provide or provides such information.

Moreover, it has been argued that the exemption is established by the issuer merely providing a brochure, or other writing, to the offerees containing the same kind of information that is found in a registration statement. The Commission is of the view that the mere disclosure of the same kind of information that would be contained in a registration statement is not sufficient in itself to establish the availability of an exemption under Section 4(2) of the Act.[5/]

It also has been argued that the private offering exemption can be established where it is represented that the securities are held for investment, where resale is restricted, and where the number of transferees is limited. In this regard, the practice has developed whereby issuers obtain investment letters from purchasers and cause a legend to be imprinted on the face of each certificate restricting transfer. As the Commission and the courts[6/] have previously stated, the signing of an investment letter and the legending of stock certificates are not sufficient to render an offering a private one. Although such precautions should be taken by issuers to protect their claim of exemption by assuring that their purchasers will not in turn distribute securities to others, these are only precautions to prevent illegal distributions and are not, by themselves, to be regarded as a sufficient basis for an exemption from registration for the issuer.

The Commission believes that a rule creating greater certainty in the application of the Section 4(2) exemption is in the public interest for two reasons. First, such a rule should deter reliance on that exemption for offerings of securities to persons who are unable to fend for themselves in terms of obtaining and evaluating information about the issuer and in certain situations, of assuming the risk of investment. These persons need the protections afforded by the registration process. Second, such a rule should reduce uncertainty to the extent feasible and provide more objective standards upon which responsible businessmen may rely in raising capital in a manner that complies with the requirements of the Act.

The Rule is designed to protect investors while at the same time providing more objective standards in order to curtail uncertainty to the extent feasible. In view of the legislative history, statutory language, judicial decisions, and the Commission's reexamination of its interpretations of Section 4(2) of the Act, the Commission is of the view that the significant concepts in determining when transactions are deemed not to involve any public offering are access to the same kind of information that registration would disclose and the ability of offerees to fend for themselves so as not to need the protections afforded by registration.

GENERAL DESCRIPTION

Rule 146 provides that transactions by an issuer involving the offer or sale of its securities shall be deemed not to involve any public offering within the meaning of Section 4(2) of the Act if they are part of an offering that meets all the conditions of the Rule. These conditions relate to limitations on the manner of offering, the nature of the offerees, access to or furnishing of information about the issuer, limitations on the number of purchasers and limitations on the subsequent disposition of securities acquired pursuant to the Rule.

First, in determining whether an offeree needs the protections afforded by registration, it is essential to consider whether the offeree has access to or has been furnished with the same kind of information that registration would disclose as well as an opportunity to acquire additional information necessary to verify that disclosure. Accordingly, conditions relating to information concerning the issuer which must be available to the offeree or his representative are included in the Rule.

Second, in order to assure that the offerees can fend for themselves, the availability of the Rule is conditioned on the nature of the offerees. Thus, the issuer and any person acting on its behalf shall have reasonable grounds to believe, and shall believe, immediately prior to making an offer, either that the offeree has such knowledge and experience that he is capable of evaluating the merits and risks of the proposed investment or that the offeree can bear the economic risk of the investment. In addition, immediately prior to a sale, the issuer and any person acting on its behalf, after making reasonable inquiry, shall have reasonable grounds to believe and shall believe either that the offeree himself has the requisite knowledge and experience, or that the offeree and his offeree representative(s) have such knowledge and experience and that the offeree himself is capable of bearing the economic risk of the investment. The concept of bearing the economic risk of the investment is not inconsistent with the discussion in Ralston Purina about the offeree's ability to fend for himself. The Rule contains special provisions in this regard for offerings in connection with certain types of business combinations.

Third, the Commission believes that there must be limitations on the manner of offering securities pursuant to the exemption to assure that persons to whom such securities are offered have the necessary information available concerning the issuer and can fend for themselves. To assure the non-public manner of the offering, the Rule precludes general advertising or general solicitation, including promotional seminars or meetings in connection with the offering. The Rule would not preclude meetings with certain qualified offerees or with certain other qualified offerees and their offeree representatives to discuss the terms of and to impart information about the offering.

Fourth, the Commission believes that a limitation on the number of purchasers serves to assure that the offering does not involve or result in a deferred distribution. Limitations on the disposition of securities are necessary to assure that the offering does not involve a series of steps resulting in a distribution.

The Rule is only available to issuers of securities and is not available to affiliates of the issuer or other persons for sales of the issuer's securities. Persons who acquire securities from issuers in transactions

complying with the Rule acquire securities that are restricted in that they can be reoffered and resold only if registered under the Act or pursuant to an exemption from such registration provisions. In this connection, Rule 144 under the Act provides objective standards for the public resale of restricted securities. (See Securities Act Release No. 5223). Rule 146 has been adopted in the context of , and in conjunction with, several rules, amendments to rules and forms, and releases which the Commission has recently adopted or issued including:

1. Rule 144 under the Act (Securities Act Release No. 5223), as amended (Securities Act Release No. 5307 and Securities Act Release No. 5452);

2. Rule 145 under the Act (Securities Act Release No. 5316);

3. Adoption of Form S-16 under the Act for securities offered in certain specified transactions (Securities Act Release No. 5217) and adoption of amendments to Form S-16 to liberalize the conditions under which the form could be used (Securities Act Release No. 5265);

4. Amendments to Regulation A under Section 3(b) of the Act (Securities Act Release No. 5225);

5. Publication of a release relating to the use of legends and stop-transfer instructions as evidence of non-public offerings (Securities Act Release No. 5121);

6. Publication of a release relating to the applicability of the anti-fraud provisions of the Securities Act to certain practices in connection with transactions by issuers and others not involving public offerings (Securities Act Release No. 5226);

7. Amendments to Forms 10-K and 10-Q under the Securities Exchange Act of 1934 (Exchange Act) to require disclosure of securities sold pursuant to Section 4(2) of the Act (Securities Exchange Act Release No. 9443);

8. Adoption of Rule 15c2-11 under the Exchange Act which requires that dealers have adequate information available concerning any issuer in whose securities they make a market (Securities Exchange Act Release No. 9310);

9. Adoption of amendments to Form 10-K to require more meaningful disclosure in reports on that Form (Securities Exchange Act Release No. 10180).

SYNOPSIS OF THE PROVISIONS OF RULE 146

Preliminary Notes

Preliminary Notes to the Rule briefly describe the Rule and make clear that all transactions which are, applying traditional integration standards, part of an offering must meet all the conditions of the Rule for it to be available. The Preliminary Notes also emphasize that compliance with all the conditions of the Rule is not the exclusive means of establishing an exemption pursuant to Section 4(2) of the Act, that attempted compliance with Rule 146 does not act as an election, that the Rule does not relieve issuers from requirements of state securities laws, and that the Rule is an

issuer's rule only. Another Preliminary Note makes clear that, for purposes of the Rule, clients of an investment adviser, customers of a broker or dealer, trusts administered by a bank trust department or persons with similar relationships will be considered to be the "offerees" or "purchasers," regardless of the amount of discretionary authority held by such investment adviser, broker or dealer, bank trust department, or other person. In addition, the Preliminary Notes restate the Commission's position, as with respect to Rules 144 and 147, that this Rule is not available to any issuer with respect to any transactions which, although in technical compliance with the Rule, are part of a plan or scheme to evade the registration provisions of the Act. In such cases registration pursuant to the Act is required.

Rule 146(a): Definitions

Offeree Representative: Rule 146(a)(1)

The term "offeree representative" is defined in subparagraph (a)(1) of the Rule as a person who the issuer and any person acting on its behalf have, after making reasonable inquiry, reasonable grounds to believe and believe is not an affiliate, director, officer or other employee, or beneficial owner of 10 percent or more of the equity of the issuer (except when the offeree is a specified relative of such person or a trust or organization with which such person and/or such relative has a specified relationship) (subdivision (i)); has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment (subdivision (ii)); is acknowledged, in writing, by the offeree during the course of the transaction to be his offeree representative (subdivision (iii)); and discloses to the offeree, in writing, any material relationship existing or mutually understood to be contemplated between himself or his affiliates and the issuer or its affiliates or any such relationship which existed during the previous two years, and any compensation received as a result of such relationship (subdivision (iv)). As was noted in the release accompanying the rule as proposed for comment in October 1973, the acknowledgment and disclosure of relationships must be made with respect to each prospective investment even in the case of a discretionary account. Where an adviser with discretionary authority wants to act as offeree representative, the Rule requires that the acknowledgment specified in subdivision (a)(1)(iii) of the Rule be obtained for each transaction. Accordingly, advance blanket acknowledgement for "all securities transactions" or "all private placements" or similar broad advance acknowledgments will not satisfy the Rule. This is particularly important, since the offeree representative is required by subdivision (a)(1)(iv) of the Rule to disclose to the offeree, in writing, any material relationships between the adviser and the issuer. This disclosure is required in connection with each offering pursuant to the Rule in order that the offeree be given an opportunity to consider any conflicts of interest the adviser may have prior to acknowledging the adviser as his offeree representative for the particular offering. A note has been added to the offeree representative definition making clear that where an offeree representative or its affiliates has a material relationship with the issuer or its affiliates, disclosure of such relationship does not relieve the offeree representative of its obligation to act in the interest of the offeree.

Several changes were made from the rule as last proposed. As proposed in October 1973, no affiliate, associate or employee of the issuer could be an offeree representative, except in specified situations; as adopted, the term "associate" has been deleted, but the definition now precludes officers and directors of the issuer, as well as 10 percent stockholders, from being offeree representatives, except in specified situations. In addition, the adopted Rule requires disclosure of any material relationship between the offeree representative or its affiliates and the issuer or its affiliates. The qualifier "material" is new to the Rule (and is defined in subparagraph (a)(4)) and disclosure of relationships with affiliates of the offeree representative is also new. The Rule also makes clear that an offeree can have more than one offeree representative. A note has been added reminding persons to consider the applicability of the Exchange Act and the Investment Advisers Act of 1940.

Issuer: Rule 146(a)(2)

For purposes of the Rule the definition of issuer in Section 2(4) of the Act applies. However, subparagraph (a)(2) includes a definition of "issuer" for purposes of offerings of certain securities in connection with proceedings under the Bankruptcy Act. The rule as proposed in October 1973 contained a definition of issuer for certain offerings involving partnerships. This has been deleted from the Rule as adopted because it was ambiguous and the Commission determined that Rule 146 was not the appropriate place to deal with that question at this time.

Affiliate: Rule 146(a)(3)

A definition of "affiliate", similar to that in Rule 144 under the Act, has been added to the Rule.

Material: Rule 146(a)(4)

A definition of "material" as it relates to the "material relationships" that must be disclosed by the offeree representative (subparagraph (a)(1)) and by the issuer (subparagraph (e)(3)) has been added to make clear that materiality is to be determined from the reasonable investor's point of view and not through some formula measuring the importance of the transaction to the offeree representative or the issuer. The definition is based on that used by the Supreme Court in Affiliated Ute Citizens of Utah v. United States (406 U.S. 128, 154, 1972).

Deletion of Proposed Rule 146(a)(2): Direct Communication

The term "direct communication" has been deleted from the Rule, although the substantive requirement of an opportunity for the offeree or his offeree representative to ask questions of, and receive answers from, the issuer or a person acting on its behalf, has been retained. The requirement is now part of paragraph (e), "Access to or Furnishing of Information."

Deletion of Proposed Rule 146(a)(3): Executive Officer

The definition of executive officer has been deleted from the definition section of the Rule because the term no longer appears in paragraph (g) of the Rule. The exclusion of "executive officers" from the count of thirty-five purchasers in a twelve month period is not necessary since the twelve month period has been abandoned as explained under paragraphs (b) and (g).

Rule 146(b): Conditions to be Met

Paragraph (b) of the Rule provides that transactions by an issuer involving the offer, offer to sell, offer for sale, or sale of securities of the issuer that are part of an offering that is made in accordance with all the conditions of the Rule are deemed to be transactions not involving any public offering within the meaning of Section 4(2) of the Act.

The Rule does not define "offering", as stated in the Preliminary Notes. In most cases, the traditional integration standards, as set forth in the Preliminary Notes, would have to be applied in order to determine what offers, offers to sell, offers for sale, and sales are part of an offering. The Rule, as adopted, does contain a safe harbor provision similar to that in Rule 147. In general, for purposes of the Rule only, an offering will be deemed not to include any offers, offers to sell, offers for sale or sales of securities of the issuer that take place prior to the six month period immediately preceding or after the six month period immediately following any offers, offers for sale, or sales pursuant to Rule 146, if during both of said six month periods there were no offers or sales of securities by or for the issuer of the same or similar class as those offered or sold pursuant to the Rule. If there were offers or sales during the six month periods before or after the offering pursuant to the Rule, the traditional integration factors set forth in Preliminary Note 3 would have to be looked to for guidance as to whether or not those offers or sales would be integrated with those made pursuant to the Rule. This concept of offering also relates specifically to the limitation on number of purchasers in paragraph (g) since that condition has been revised to limit to thirty-five the number of purchasers in any offering, as opposed to in any twelve month period, as proposed.

Rule 146(c): Limitations on Manner of Offering

Paragraph (c) of the Rule specifies limitations on the manner in which the securities can be offered and sold. The Rule prohibits the issuer or any person acting on its behalf from offering or selling the securities through any form of general advertising or general solicitation including, but not limited to advertisements or other communications in newspapers, magazines, or other media; broadcasts on radio or television; seminars or promotional meetings or any letter, circular, or other written communication.

The prohibition on general advertising and general solicitation does not necessarily mean that there can be no meetings or written communication. It means that any such meetings can involve only offerees and their offeree representatives who can satisfy the conditions of paragraph (d), "Nature of Offerees," and that any written material can be distributed only to offerees who satisfy the conditions of paragraph (d) and only if such communications contain an undertaking to provide the information specified in subparagraph (e)(1) on request. Of course, any person acting on behalf of the issuer can attend such meetings or seminars without satisfying the conditions of paragraph (d), assuming that he is not and will not become an offeree. The substance of the requirement that there be direct communication has been moved from paragraph (c) of the Rule to paragraph (e), "Access to and Furnishing of Information."

Rule 146(d): Nature of Offerees

Subparagraph (d)(1) of the Rule requires that the issuer and any person acting on its behalf shall have reasonable grounds to believe and shall believe immediately prior to making an offer either that the offeree has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or that an offeree can bear the economic risk of the investment. Subparagraph (d)(2) requires that immediately prior to making a sale, the issuer and any person acting on its behalf, after making reasonable inquiry, shall have reasonable grounds to believe and shall believe either (1) that the offeree has the requisite knowledge and experience, or (2) that the offeree and his offeree representative(s) have the requisite knowledge and experience and that the offeree is a person who is able to bear the economic risk of the investment.

The Commission has determined to retain the economic risk test for offerees who need the knowledge and experience of an offeree representative in order to be qualified purchasers. This is necessary in order to control the types of persons to whom offers can be made. The Commission believes that the determination of "ability to bear the economic risk" will vary with the circumstances. Important considerations are whether the offeree could afford to hold unregistered securities for an indefinite period, and whether, at the time of the investment, he could afford a complete loss.

The structure of subparagraphs (d)(1) and (d)(2) has been changed from the rule as proposed so that the sequence of events is clearer. The substance, however, is not significantly different. In addition, the requirement that the issuer make reasonable inquiry as to the offeree's qualifications prior to sale to the offeree has been made explicit. If, as a result of inquiry after the offer, but before the sale, or otherwise, the issuer discovers that the offeree was not qualified, the Rule is still available as to the offer if the issuer had reasonable grounds to believe and believed, immediately prior to making the offer, that the offeree was qualified.

The same would be true if it is discovered after a sale that the purchaser did not in fact meet the standards of subparagraph (d)(2), as long as the issuer had had reasonable grounds to believe, and had believed, that the offeree met the standards of subparagraph (d)(1) and, after making reasonable inquiry, that he met the standards of subparagraph (d)(2). The rule as proposed contained a subparagraph (d)(3) which was an attempt to clarify the above point. However, subparagraph (d)(3) has been deleted because it was extraneous.

Rule 146(e): Access to or Furnishing of Information

Paragraph (e) of the Rule requires that the offeree have access to the same kind of information that is required by Schedule A of the Act to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense (subdivision (e)(1)(i)) or that the offeree or his offeree representative be furnished, during the course of the transaction and prior to sale, such information (subdivision (e)(1)(ii)). The term "access" is used in the Rule in the same sense that it has been used by courts and the Commission in the past--to refer to the offeree's position with respect to the issuer. This position can only exist because of an employment or family relationship or economic bargaining power that enables a person to obtain information from the issuer in order to evaluate the merits and risks of the prospective investment. A note to the Rule reflects the foregoing.

In addition, the offeree or his offeree representative must have available to him the opportunity to obtain any additional information necessary to verify the accuracy of the information obtained pursuant to subparagraph (e)(1) to the extent the issuer possesses such information or can acquire it without unreasonable effort or expense (subparagraph (e)(2)). The direct communication requirement in paragraph (c) of the rule as proposed was incorporated in substance into subparagraph (e)(2) where it is more relevant. Such verification and opportunity for communication are appropriate in view of the absence of the statutory safeguards and sanctions attendant to the registration process, as well as the absence of traditional underwriter's due diligence. An explanatory note to this paragraph makes clear that information need not be continued to be furnished nor the opportunities for verification continued with respect to those offerees who have indicated that they are not interested in purchasing the securities offered, or to those to whom the issuer or any person acting on its behalf has determined not to sell (except where an undertaking was made pursuant to subparagraph (c)(3)).

In order to provide standards for the types of information that would satisfy the conditions of subdivision (e)(1)(ii), the Rule has been revised to specify more meaningfully the information required to be furnished by reporting and non-reporting issuers. An issuer subject to the reporting provisions of the Exchange Act may satisfy the provisions of subdivision (e)(1)(ii) by providing each offeree or his representative with the information contained in the annual report required to be filed under that Act or in a registration statement on Form S-1 under the Act, or on Form 10 under the Exchange Act, whichever is the most recent required to be filed. In addition, the issuer must provide the information contained in any

definitive proxy statement required to be filed, and in any reports or documents required to be filed by the issuer in compliance with Section 13 or 15(d) of the Exchange Act, since the filing of the annual report or registration statement. The issuer must also provide each offeree with a brief description of the securities being offered, the intended use of proceeds and any material changes in the issuer's affairs not disclosed in the forms filed. The Rule permits the information to be provided to offerees in one document, such as an offering circular, since the combined document may make the information more readily understandable.

Non-reporting issuers may satisfy subdivision (e)(1)(ii) by providing the information specified by the registration statement form which the issuer would be entitled to use, except that where certified financial statements are not available and cannot be obtained without unreasonable effort or expense, they may be provided on an unaudited basis.

A new subdivision of the Rule, (e)(1)(ii)(c), provides that exhibits required to be filed with registration statements and reports need not be given to the offeree or his representative as long as such exhibits are described and are available for inspection pursuant to subparagraph (e)(2).

Subparagraph (e)(3) requires, as it did in the proposal, that the issuer or any person acting on its behalf inform each offeree prior to sale and in writing, of the need to bear the economic risk of investment because the securities are not registered and of the restrictions on resale. In addition, the Rule now requires that the issuer or any person acting on its behalf disclose to each offeree, prior to sale, in writing, any material relationship between the offeree's offeree representative or its affiliates and the issuer or its affiliates of the type described in subdivision (a)(1)(iv). This additional requirement has been added because of the importance of this disclosure and because the burden for complying with the Rule must ultimately rest on the issuer.

Rule 146(f): Business Combinations

Paragraph (f) of the Rule on business combinations has been substantially revised in form, although the substance is similar to that in the rule as last proposed for comment. Instead of including a definition of "business combination" in the rule itself, the Rule now refers to any transaction of the type described in paragraph (a) of Rule 145. The Rule 145 definition of business combination does not include an exchange offer although the October 1973 Rule 146 proposal did. In an exchange offer the issuer has a choice of offerees and, therefore, does not need the special provisions of paragraph (f).

Subparagraph (f)(2) of the Rule provides that paragraph (d) of the Rule, "Nature of Offerees," does not apply to business combinations, but subparagraph (f)(3) goes on to require that the issuer and any person acting on its behalf, after making reasonable inquiry, shall have reasonable grounds to believe and shall believe, prior to the submission of any plan for a business combination to security holders for their approval, that each offeree alone or with his offeree representative(s) has the requisite knowledge and experience. Subparagraph (f)(3) means that an offeree who needs an offeree representative in order to satisfy the knowledge and experience test, and who refuses to have one, may make the Rule unavailable for the transaction. Numerous comments on this point were received in sponse to a similar condition in the rule as last proposed. Although the Commission is aware of the possible problems this may cause, the Commission does not believe that it can allow satisfaction of the state corporate law requirements as to business combinations to replace satisfaction of the federal securities laws. The Rule has been revised, however, to provide that subparagraph (h)(4), which requires a written agreement from the purchaser that the securities will not be sold without registration or an exemption therefrom, will not apply to business combinations because of the difficulty of obtaining such an agreement in some cases where the purchasers are a group over which the issuer has no control. The securities acquired are restricted, however, in the same manner as other securities acquired pursuant to the Rule, and the issuer, for its own protection, should consider obtaining appropriate letters. The Rule also provides that the issuer must, in connection with the information furnished pursuant to subparagraph (e)(3), inform each offeree in writing about any terms of the transaction relating to any security holder that are not proposed to be identical to those relating to all other security holders (subparagraph (f)(4)).

The rule as proposed contained a provision that certain written communications would be deemed not to be "offers" for purposes of a business combination. We have deleted this provision since we believe it is no longer relevant in view of new subparagraph (f)(3).

Rule 146(g): Number of Purchasers

The Rule as last proposed provided that in any consecutive twelve month period there could be no more than thirty-five persons who purchased securities of the issuer of the same or similar class pursuant to the rule, or otherwise in reliance on Section 4(2). The proposed rule also set forth various classes of purchasers who would not be included in counting the thirty-five. The Commission has decided that the thirty-five purchasers

in twelve month test is too rigid and involves too many exceptions to be useful. In addition, it would have made it difficult for an issuer to know when the rule was available since it would have had to wait twelve months after every sale. Therefore, as described under Rule 146(b), "Conditions to Be Met," the Rule is now based on the traditional concept of "an offering" and subparagraph (g)(1) now requires that there be no more than thirty-five purchasers in any offering pursuant to the Rule. In order to determine what constitutes "an offering," reference would have to be made to the traditional integration standards, as set forth in a Preliminary Note. In addition, subparagraph (b)(1) of the Rule provides a safe harbor for certain offers and sales. Reliance on the traditional integration standards means that the various exclusions for directors and officers, bank lenders, subsidiaries, employee plans and business combinations are no longer necessary. The specific exclusions were only necessary when all sales of the same or similar class of securities during a twelve month period were automatically integrated.

In the Rule as adopted there are specific provisions for calculating the thirty-five purchasers. Subdivision (g)(2)(i) of the Rule, as adopted, indicates that for purposes of computing the number of purchasers, some purchasers would be excluded: certain relatives of a purchaser, trusts and estates in which the purchaser and such relatives own all of the beneficial interest and corporations or other organizations in which the purchaser and such relatives are beneficial owners of all of each class of equity securities or all of the equity interest. As in the rule as last proposed, for purposes only of counting the number of purchasers, those who purchase or agree in writing to purchase, for cash in a single payment or installments, securities for $150,000 or more would be excluded. However, the issuer would have to satisfy all the other provisions of the Rule with respect to such persons.

Subdivision (g)(2)(ii) provides that corporations, partnerships, trusts and certain other entities will be counted as one purchaser unless the entity was formed for the specific purpose of acquiring the securities offered, in which case each beneficial owner of an equity interest in the entity would be counted as a separate purchaser.

The rule as proposed would have treated clients of an investment adviser as separate persons in determining the number of persons to whom securities could be sold, regardless of the amount of discretion given to the investment adviser to act on behalf of the client in purchasing securities. The Commission received many comments suggesting that an investment adviser, broker-dealer or trust department that purchases securities for discretionary or advisory accounts should count as only one person for purposes of the Rule. Having reviewed the comments and considered the matter, the Commission still believes that, in order to avoid the possibility of a

distribution, it is necessary to count each purchaser as a separate person for purposes of paragraph (g). This position is now set forth in Preliminary Note 5, discussed above. In determining the number of purchasers in an offering pursuant to the Rule each client of an investment adviser, each customer of a broker-dealer and each trust administered by a bank trust department will be counted as a separate purchaser. Pursuant to subdivision (g)(2)(ii), investment companies or pension or other trusts will be counted as one purchaser. However, each trust or investment company or group of trusts or investment companies under common management will be treated as a separate purchaser.

Rule 146(h): Limitations on Disposition

The Rule also provides that the issuer and any person acting on its behalf must take reasonable care to assure that the purchasers are not underwriters. Such reasonable care shall include but is not necessarily limited to (1) making reasonable inquiry to determine if the purchaser is purchasing for his own account or on behalf of others; (2) placing a legend on the certificates or other documents evidencing the securities indicating that they were not registered and setting forth or referring to the restrictions on transferability and sale; (3) issuing stop transfer instructions to the transfer agent, if any, or making an appropriate notation in the issuer's records if the issuer transfers its own securities; and (4) except as provided in subparagraph (f)(2), obtaining a written agreement from the purchaser that the securities will not be resold without registration or exemption therefrom. The Commission believes that these limitations are necessary in order to protect the public from a deferred distribution. They are also in the self interest of the issuer.

Deletion of Proposed Rule 146(i): Report of Sale

The Commission has decided to delete the requirement that a report of sales made pursuant to Rule 146 be filed on Form 146. As the rule was last proposed, a report of sales had to be filed within 45 days after the end of any quarter of the issuer's fiscal year during which certain sales were effected pursuant to the proposed Rule. The Commission has determined that requiring the filing of such a Form as a condition of the Rule would unnecessarily increase the difficulty of complying with the Rule for many small issuers. In addition, filing requirements would generally affect only non-public companies, since public companies already supply similar information in their Form 10-Q and Form 10-K filings under the Exchange Act. The Commission will reexamine the need for a filing requirement after experience with the Rule has been gained, and if appropriate for the protection of investors and in the public interest, will propose amendments to the Rule to require such forms

OPERATION OF RULE 146

The Rule will operate prospectively only starting from its effective date, June 10, 1974. Further, the staff will issue interpretive letters to assist persons in complying with the Rule. Although the staff will continue to consider no-action requests relating to Section 4(2) of the Act, such letters will only be issued infrequently and only in the most compelling circumstances.

The Commission recognizes that no one rule can adequately cover all legitimate private offerings and sales of securities. It is to be emphasized that the Rule does not provide the exclusive means for offering and selling securities in reliance on Section 4(2). Issuers who satisfy the criteria set forth in relevant judicial and administrative interpretations of Section 4(2) in effect at the time of a proposed transaction may offer and sell without compliance with the Rule. In addition, it should be noted that attempted compliance with Rule 146 does not act as an election so that the issuer can always claim the protection of both the Rule and Section 4(2), but will have the burden of proving the availability of the exemption.

The courts and the Commission have consistently held that one claiming an exemption under Section 4(2) of the Act has the burden of proving that the exemption is available to him and the Rule does not shift that burden. In addition, it should be pointed out that the burden of proof applies with respect to each offeree and not just to the purchasers of the securities. See Lively v. Hirschfeld, 440 F. 2d 631 (10th Cir. 1971). Accordingly, any issuer who relies on the Rule has the burden of establishing that it has satisfied all the conditions of the Rule. Such issuer for its own protection should obtain and retain in its files written evidence that would assist in meeting this evidentiary burden.

The Commission has determined not to include within the terms and conditions of Rule 146 specific standards for determining whether a private offering should be regarded as a part of a larger public offering for which the exemption provided by Section 4(2) would not be available. The Commission rather has determined that its existing guidelines relating to integration of offerings as set forth in Securities Act Release No. 4552 7/ should apply to offerings made pursuant to Rule 146. The Commission believes that the following factors discussed in that Release are relevant to the question of integration: whether (1) the offerings are part of a single plan of financing, (2) the offerings involve issuance of the same class of security, (3) the offerings are made at or about the same time, (4) the same type of consideration is to be received, and (5) the offerings are made for the same general purpose.

In view of the objectives and policies underlying the Act, the Rule is not available to any issuer with respect to any transaction which, although in technical compliance with the provisions of the Rule, is part of a plan or scheme to evade the registration provisions of the Act. In such case, registration is required.

Rule 146 relates to transactions exempted by Section 4(2) of the Act from the registration provisions of Section 5; it does not provide an exemption from the anti-fraud provisions of the securities laws or the civil liabilities provisions of Section 12(2) of the Act or other provisions of the securities laws. In addition, investment companies or persons acting on their behalf proposing to offer or sell securities in reliance on the Rule should carefully consider all applicable provisions of the Investment Company Act of 1940 before proceeding.

The Rule is available only to the issuer of the securities and not to affiliates or other persons reselling or otherwise disposing of securities of the issuer. Such disposition must be made in compliance with the registration provisions of the Act unless an exemption from such provisions is available. Also, the Rule does not relieve issuers of their obligations under relevant state laws.

It should be recognized that the Rule is intended to be in the nature of an experiment and that the Commission will observe its operation to determine whether it is consistent with the objectives of the Act. If experience with the proposed Rule indicates that it is not operating for the protection of investors or in the public interest, it will be rescinded or appropriately amended.

The Commission hereby adopts Rule 146 pursuant to Sections 4(2) and 19(a) of the Securities Act of 1933, as amended, effective June 10, 1974 for offerings commencing on or after that date. The Commission finds that the changes reflected in the Rule as adopted, from the rule as last proposed for comment, are technical or generally have already been subject to public comment, and that further notice and other rule making procedures pursuant to the Administrative Procedure Act are not necessary.

The text of Rule 146 is attached hereto.

By the Commission.

George A. Fitzsimmons
Secretary

1/ H.R. Rep. No. 85, 73rd Cong., 1st Sess. 5 (1933).

2/ The House Report does indicate that the exemption was originally intended to permit an issuer to make a specific or isolated sale of its securities to a particular person or financial institution. Id. at p. 15-16.

3/ SEC v. Ralston Purina Co., 346 U.S. 119 (1953).

4/ United States v. Custer Channel Wing Corp., 376 F. 2d 675 (4th Cir. 1967); SEC v. Tax Service, Inc., 357 F. 2d 143 (4th Cir. 1966).

5/ See SEC v. Continental Tobacco Company of South Carolina, Inc., 463 F. 2d 137 (5th Cir. 1972); Hill York Corp. v. Freeman, 448 F. 2d 680 (5th Cir. 1971).

6/ Securities Act Release No. 5121 (December 30, 1970); United States v. Custer Channel Wing, 376 F. 2d 675 (4th Cir. 1967).

7/ Issued November 6, 1962.

Rule 146. Transactions by an Issuer Deemed Not to Involve Any Public Offering

Preliminary Notes

1. The Commission recognizes that no one rule can adequately cover all legitimate private offers and sales of securities. Transactions by an issuer which do not satisfy all of the conditions of this rule shall not raise any presumption that the exemption provided by Section 4(2) of the Act is not available for such transactions. Issuers wanting to rely on that exemption may do so by complying with administrative and judicial interpretations in effect at the time of the transactions. Attempted compliance with this rule does not act as an election; the issuer can also claim the availability of Section 4(2) outside the rule.

2. Nothing in this rule obviates the need for compliance with any applicable state law relating to the offer and sale of securities.

3. Section 5 of the Act requires that all securities offered by the use of mails or other channels of interstate commerce be registered with the Commission. Congress, however, provided certain exemptions in the Act from such registration provisions where there was no practical need for registration or where the public benefits of registration were too remote. Among these exemptions is that provided by Section 4(2) of the Act for transactions by an issuer not involving any public offering. The courts and the Commission have interpreted the Section 4(2) exemption to be available for offerings to persons who have access to the same kind of information that registration would provide and who are able to fend for themselves. The indefiniteness of such terms as "public offering", "access" and "fend for themselves" has led to uncertainties with respect to the availability of the Section 4(2) exemption. Rule 146 is designed to provide, to the extent feasible, objective standards upon which responsible businessmen may rely in raising capital under claim of the Section 4(2) exemption and also to deter reliance on that exemption for offerings of securities to persons who need the protections afforded by the registration process.

In order to obtain the protection of the rule, all its conditions must be satisfied and the issuer claiming the availability of the rule has the burden of establishing, in an appropriate forum, that it has satisfied them. The burden of proof applies with respect to each offeree as well as each purchaser. See Lively v. Hirschfeld, 440 F. 2d 631 (10th Cir. 1971). Broadly speaking, the conditions of the rule relate to limitations on the manner of the offering, the nature of the offerees, access to or furnishing of information, the number of purchasers, and limitations on disposition.

The term "offering" is not defined in the rule. The determination as to whether offers, offers to sell, offers for sale, or sales of securities are part of an offering (i.e., are deemed to be "integrated") depends on the particular facts and circumstances. See Securities Act Release No. 4552 (November 6, 1962). All offers, offers to sell, offers for sale, or sales which are part of an offering must meet all of the conditions of Rule 146 for the rule to be available. Release 33-4552 indicates that in determining whether offers and sales should be regarded as a part of a larger offering and thus should be integrated, the following factors should be considered:

(a) whether the offerings are part of a single plan of financing;

(b) whether the offerings involve issuance of the same class of security;

(c) whether the offerings are made at or about the same time;

(d) whether the same type of consideration is to be received; and

(e) whether the offerings are made for the same general purpose.

4. Rule 146 relates to transactions exempted from Section 5 by Section 4(2) of the Act. It does not provide an exemption from the anti-fraud provisions of the securities laws or the civil liability provisions of Section 12(2) of the Act or other provisions of the securities laws, including the Investment Company Act of 1940.

5. Clients of an investment adviser, customers of a broker or dealer, trusts administered by a bank trust department or persons with similar relationships shall be considered to be the "offerees" or "purchasers" for purposes of the rule regardless of the amount of discretion given to the investment adviser, broker or dealer, bank trust department or other person to act on behalf of the client, customer or trust.

6. The rule is available only to the issuer of the securities and is not available to affiliates or other persons for sales of the issuer's securities.

7. Finally, in view of the objectives of the rule and the purposes and policies underlying the Act, the rule is not available to any issuer with respect to any transactions which, although in technical compliance with the rule, are part of a plan or scheme to evade the registration provisions of the Act. In such cases registration pursuant to the Act is required.

RULE 146

(a) Definitions. The following definitions shall apply for purposes of this rule.

(1) Offeree Representative. The term "offeree representative" shall mean any person or persons, each of whom the issuer and any person acting on its behalf, after making reasonable inquiry, have reasonable grounds to believe and believe satisfies all of the following conditions:

(i) is not an affiliate, director, officer or other employee of the issuer, or beneficial owner of 10 percent or more of any class of the equity securities or 10 percent or more of the equity interest in the issuer, except where the offeree is:

(a) related to such person by blood, marriage or adoption, no more remotely than as first cousin;

(b) any trust or estate in which such person or any persons related to him as specified in subdivision (a) or (c) collectively have 100 percent of the beneficial interest (excluding contingent interests) or of which any such person serves as trustee, executor, or in any similar capacity; or

(c) any corporation or other organization in which such person or any persons related to him as specified in subdivision (a) or (b) collectively are the beneficial owners of 100 percent of the equity securities (excluding directors' qualifying shares) or equity interest;

(ii) has such knowledge and experience in financial and business matters that he, either alone, or together with other offeree representatives or the offeree, is capable of evaluating the merits and risks of the prospective investment:

(iii) is acknowledged by the offeree, in writing, during the course of the transaction, to be his offeree representative in connection with evaluating the merits and risks of the prospective investment; and

(iv) discloses to the offeree, in writing, prior to the acknowledgement specified in subdivision (iii), any material relationship between such person or its affiliates and the issuer or its affiliates, which then exists or is mutually understood to be contemplated or which has existed at any time during the previous two years, and any compensation received or to be received as a result of such relationship.

NOTE 1: Persons acting as offeree representatives should consider the applicability of the registration and anti-fraud provisions relating to brokers and dealers under the Securities Exchange Act of 1934 and relating to investment advisers under the Investment Advisers Act of 1940.

NOTE 2: The acknowledgment required by subdivision (iii) and the disclosure required by subdivision (iv) must be made with specific reference to each prospective investment. Advance blanket acknowlegment, such as for "all securities transactions" or "all private placements", is not sufficient.

NOTE 3: Disclosure of any material relationships between the offeree representative or its affiliates and the issuer or its affiliates does not relieve the offeree representative of its obligation to act in the interest of the offeree.

(2) Issuer. The definition of the term "issuer" in Section 2(4) of the Act shall apply, provided that notwithstanding that definition, in the case of a proceeding under the Bankruptcy Act, the trustee, receiver, or debtor in possession shall be deemed to be the issuer in an offering for purposes of a plan of reorganization or arrangement, if the securities offered are to be issued pursuant to the plan, whether or not other like securities are offered under the plan in exchange for securities of, or claims against, the debtor.

(3) Affiliate. The term "affiliate" of a person means a person that directly or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with such person.

(4) Material. The term "material" when used to modify "relationship" means any relationship that a reasonable investor might consider important in the making of the decision whether to acknowledge a person as his offeree representative.

(b) Conditions to be Met. Transactions by an issuer involving the offer, offer to sell, offer for sale or sale of securities of the issuer that are part of an offering that is made in accordance with all the conditions of this rule shall be deemed to be transactions not involving any public offering within the meaning of Section 4(2) of the Act.

(1) For purposes of this rule only, an offering shall be deemed not to include offers, offers to sell, offers for sale or sales of securities of the issuer pursuant to the exemptions provided by Section 3 or Section 4(2) of the Act or pursuant to a registration statement filed under the Act, that take place prior to the six month period immediately preceding or after the six month period immediately following any offers, offers for sale or sales pursuant to this rule, provided, that there are during neither of said six month periods any offers, offers for sale or sales of securities by or for the issuer of the same or similar class as those offered, offered for sale or sold pursuant to the rule.

NOTE: In the event that securities of the same or similar class as those offered pursuant to the rule are offered, offered for sale or sold less than six months prior to or subsequent to any offer, offer for sale or sale pursuant to the rule, see Preliminary Note 3 hereof as to which offers, offers to sell, offers for sale or sales may be deemed to be part of the offering.

(c) Limitations on Manner of Offering. Neither the issuer nor any person acting on its behalf shall offer, offer to sell, offer for sale, or sell the securities by means of any form of general solicitation or general advertising, including but not limited to, the following:

(1) Any advertisement, article, notice or other communication published in any newspaper, magazine or similar medium or broadcast over television or radio;

(2) Any seminar or meeting, except that if subparagraph (d)(1) is satisfied as to each person invited to or attending such seminar or meeting, and, as to persons qualifying only under subdivision (d)(1)(ii), such persons are accompanied by their offeree representative(s), then such seminar or meeting shall be deemed not to be a form of general solicitation or general advertising; and

(3) Any letter, circular, notice or other written communication, except that if subparagraph (d)(1) is satisfied as to each person to whom the communication is directed and the communication contains an undertaking to provide the information specified by subparagraph (e)(1) on request, such communication shall be deemed not to be a form of general solicitation or general advertising.

(d) Nature of Offerees. The issuer and any person acting on its behalf who offer, offer to sell, offer for sale or sell the securities shall have reasonable grounds to believe and shall believe:

(1) immediately prior to making any offer, either:

(i) that the offeree has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or

(ii) that the offeree is a person who is able to bear the economic risk of the investment

; and

(2) immediately prior to making any sale, after making reasonable inquiry, either:

(i) that the offeree has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or

(ii) that the offeree and his offeree representative(s) together have such knowledge and experience in financial and business matters that they are capable of evaluating the merits and risks of the prospective investment and that the offeree is able to bear the economic risk of the investment.

(e) Access to or Furnishing of Information.

NOTE: Access can only exist by reason of the offeree's position with respect to the issuer. Position means an employment or family relationship or economic bargaining power that enables the offeree

to obtain information from the issuer in order to evaluate the merits and risks of the prospective investment.

(1) Either

(i) each offeree shall have access during the course of the transaction and prior to the sale to the same kind of information that is specified in Schedule A of the Act, to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense; or

(ii) each offeree or his offeree representative(s), or both, shall have been furnished during the course of the transaction and prior to sale, by the issuer or any person acting on its behalf, the same kind of information that is specified in Schedule A of the Act, to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense. This condition shall be deemed to be satisfied as to an offeree if the offeree or his offeree representative is furnished with information, either in the form of documents actually filed with the Commission or otherwise, as follows:

(a) in the case of an issuer that is subject to the reporting requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934:

(1) the information contained in the annual report required to be filed under the Exchange Act or a registration statement on Form S-1 under the Act or on Form 10 under the Exchange Act, whichever filing is the most recent required to be filed, and the information contained in any definitive proxy statement required to be filed pursuant to Section 14 of the Exchange Act and in any reports or documents required to be filed by the issuer pursuant to Section 13(a) or 15(d) of the Exchange Act, since the filing of such annual report or registration statement, and

(2) a brief description of the securities being offered, the use of the proceeds from the offering, and any material changes in the issuer's affairs which are not disclosed in the documents furnished;

(b) in the case of all other issuers, the information that would be required to be included in a registration statement filed under the Act on the form which the issuer would be entitled to use, provided, however, that if the issuer does not have the audited financial statements required by such form and cannot obtain them without unreasonable effort or expense, such financial statements may be provided on an unaudited basis;

(c) notwithstanding subdivisions (e)(1)(ii)(a) and (b) exhibits required to be filed with the Commission as part of a registration statement or report need not be furnished to each offeree or offeree representative if the contents of the exhibits are identified and such exhibits are available pursuant to subparagraph (e)(2)

; and

(2) The issuer shall make available, during the course of the transaction and prior to sale, to each offeree or his offeree representative(s) or both, the opportunity to ask questions of, and receive answers from, the issuer or any person acting on its behalf concerning the terms and conditions of the offering and to obtain any additional information, to the extent the issuer possesses such information or can acquire it without unreasonable effort or expense, necessary to verify the accuracy of the information obtained pursuant to subparagraph (e)(1) above; and

(3) The issuer or any person acting on its behalf shall disclose to each offeree, in writing, prior to sale:

(i) any material relationship between his offeree representative(s) or its affiliates and the issuer or its affiliates, which then exists or mutually is understood to be contemplated or which has existed at any time during the previous two years, and any compensation received or to be received as a result of such relationship;

(ii) that a purchaser of the securities must bear the economic risk of the investment for an indefinite period of time because the securities have not been registered under the Act and, therefore, cannot be sold unless they are subsequently registered under the Act or an exemption from such registration is available; and

(iii) the limitations on disposition of the securities set forth in subparagraphs (h)(2), (h)(3), and (h)(4) of the rule

NOTE: Information need not be provided and opportunity to obtain additional information need not be continued to be provided to any offeree or offeree representative who, during the course of the transaction, indicates that he is not interested in purchasing the securities offered, or, except in the case of any undertaking made pursuant to subparagraph (c)(3), to whom the issuer or any person acting on its behalf has determined not to sell the securities

(f) Business Combinations.

(1) The term "business combination" shall mean any transaction of the type specified in paragraph (a) of Rule 145 under the Act.

(2) All the conditions of this rule except paragraph (d) and subparagraph (h)(4) shall apply to business combinations.

NOTE: Notwithstanding the absence of a written agreement pursuant to subparagraph (h)(4), any securities acquired in an offering pursuant to paragraph (f) are restricted and may not be resold without registration under the Act or an exemption therefrom.

(3) For purposes of paragraph (f) only, the issuer and any person acting on its behalf after making reasonable inquiry, shall have reasonable grounds to believe, and shall believe, at the time that any plan for a business combination is submitted to security holders for their approval, that each offeree either alone or with his offeree representative(s) has such knowledge and experience in financial and business matters that he is or they are capable of evaluating the merits and risks of the prospective investment.

(4) In addition to information required by paragraph (e), the issuer shall provide, in writing, to each offeree at the time the plan is submitted to security holders for approval, information about any terms or arrangements of the proposed transaction relating to any security holder that are not identical to those relating to all other security holders.

(g) Number of Purchasers.

(1) There shall be no more than thirty-five purchasers of the securities of the issuer from the issuer in any offering pursuant to the rule.

NOTE: See subparagraph (b)(1), the note thereto and the Preliminary Notes as to what may or may not constitute an offering pursuant to the rule.

(2) For purposes of computing the number of purchasers for subparagraph (g)(1) only:

(i) the following purchasers shall be excluded:

(a) any relative or spouse of a purchaser and any relative of such spouse, who has the same home as such purchaser; and

(b) any trust or estate in which a purchaser or any of the persons related to him as specified in subdivision (g)(2)(i)(a) or (c) collectively have 100 percent of the beneficial interest (excluding contingent interests);

(c) any corporation or other organization of which a purchaser or any of the persons related to him as specified in subdivision (g)(2)(i)(a) or (b) collectively are the beneficial owners of all the equity securities (excluding directors' qualifying shares) or equity interest; and

(d) any person who purchases or agrees in writing to purchase for cash in a single payment or installments, securities of the issuer in the aggregate amount of $150,000 or more.

NOTE: The issuer would have to satisfy all the other provisions of the rule with respect to the purchasers specified in subdivision (g)(2)(i).

(ii) There shall be counted as one purchaser any corporation, partnership, association, joint stock company, trust or unincorporated organization, except that if such entity was organized for the specific purpose of acquiring the securities offered, each beneficial owner of equity interests or equity securities in such entity shall count as a separate purchaser.

NOTE: See Preliminary Note 5 as to other persons who are considered to be purchasers.

(h) Limitations on Disposition. The issuer and any person acting on its behalf shall exercise reasonable care to assure that the purchasers of the securities in the offering are not underwriters within the meaning of Section 2(11) of the Act. Such reasonable care shall include, but not necessarily be limited to, the following:

(1) making reasonable inquiry to determine if the purchaser is acquiring the securities for his own account or on behalf of other persons;

(2) placing a legend on the certificate or other document evidencing the securities stating that the securities have not been registered under the Act and setting forth or referring to the restrictions on transferability and sale of the securities;

(3) issuing stop transfer instructions to the issuer's transfer agent, if any, with respect to the securities, or, if the issuer transfers its own securities, making a notation in the appropriate records of the issuer; and

(4) obtaining from the purchaser a signed written agreement that the securities will not be sold without registration under the Act or exemption therefrom.

NOTE: Subparagraph (h)(4) does not apply to business combinations as described in paragraph (f). Notwithstanding the absence of a written agreement, the securities are restricted and may not be resold without registration under the Act or an exemption therefrom. The issuer for its own protection should consider, however, obtaining such written agreement even in business combinations.